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SECOND QUARTER 2001
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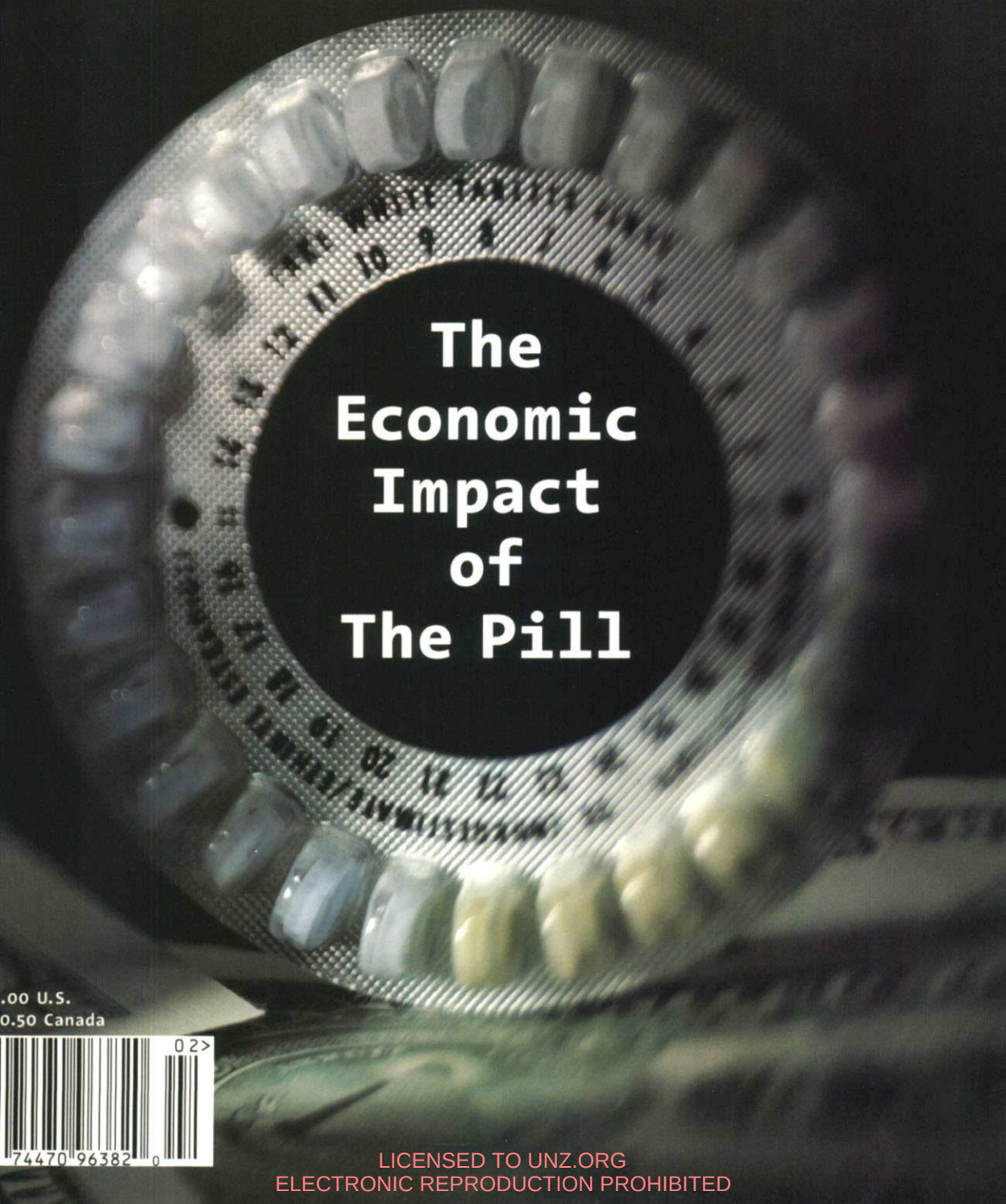

The Economic Impact of The Pill

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THE MILKEN INSTITUTE REVIEW • SECOND QUARTER 2001

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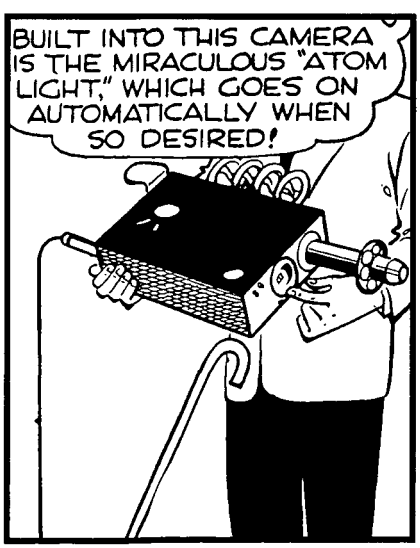

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We're in double digits!

Yes, devoted readers and the rest of you, this is the 10th issue of *The Milken Institute Review*. And it's a winner, if I do say so myself.

Irony, as ever, is our specialty. And **Rob Norton**, the former economics editor of *Fortune*, kicks off the issue with the tale of how Republicans and Democrats have reversed roles on fiscal policy over the last two decades. Read it and weep – or giggle – the story deserves a bit of each.

They say sex sells magazines. Our lead piece by **Claudia Goldin** and **Larry Katz** of Harvard isn't likely to pique the interest of teenage males in heat. But it should serve as a startling reminder of how the technology of contraception paved the way for the entry of women into the commanding heights of the labor force. "Beginning in the late 1960s," they explain, "reliable female-controlled contraception enhanced the ability and willingness of young women to enter careers that involved extensive and upfront time commitments in education." The rest is herstory.

What's black and white, and read all... Whoops, wrong riddle. What can't be seen, touched or tasted, and is worth more money than all the pardons issued by Bill Clinton combined? The electromagnetic spectrum, or at least the portion that can be used for telecommunications. **Larry White**, an economist at New York University's Stern School of Business, asks whether it isn't time – indeed, long past time – to stop pretending the spectrum is public property when it has already been unofficially privatized by muscular squatters ranging from GE to Disney.

"Any change in a decades-old public policy that affects every American in some way and some influential Americans in very big ways would be hard to change," White writes. "But if – and this is a big 'if' – a wider constituency could be convinced that the productivity gains associated with more efficient use of spectrum were large enough to offer widespread benefits reasonably rapidly, change might be possible."

The sound of car alarms is so common that few people notice them any more. What you may not know, though, is that home burglar alarms misfire almost as frequently. And, in spite of the fact that at least 19 out of 20 are false alarms, police respond dutifully at enormous cost to local taxpayers. **Erwin Blackstone** and **Simon Hakim** of Temple University, and **Uriel Spiegel** of Bar Ilan University in Israel offer the false alarm problem as a case study in how to create incentives for the efficient production of services that have both a public and private purpose.

"The solutions implemented by police departments and the alarm industry have, at best, put a Band-Aid on the false alarm problem," they say. "The problem can be overcome only if the hybrid nature of the service is recognized, and an appropriate competitive

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market solution for the private segment of the service is implemented."

If you're one of those people who think economics is all work and no play, consider the example of **Alan Krueger** of Princeton University who went to the Super Bowl this year and wrote off his expenses as a tax deduction. Legitimately, by the way, as you shall see in his ruminations on the market for Super Bowl tickets.

Why, he asks, does the National Football League sell the tickets for a fraction of their free market value, leaving thousands of die-hard fans to the mercies of scalpers? Krueger isn't quite sure. But he has a lot of ideas, and his piece offers a nice glimpse into the way a first-rate economist tries to reconcile the standard model of economic rationality with real-world events.

"Globalism" has become a snooze word – the sort you're likely to associate with headlines on *The New York Times* OpEd page.* We all know it's terribly important, but we'd all rather be doing something other than reading about it. This month's book excerpt from **Barbara Garson's** *Money Makes the World Go Round*, rises to the challenge of making globalism interesting as well as important. She traces the impact of her own modest investment in a savings account, which among others things, finances oil refinery equipment in Singapore.

A sample: "You can think of petroleum refining like hog butchering. They hack the ribs off for chops, the belly for bacon, the thighs for ham, the guts for chitterlings, and grind the bones into fertilizer."

Like mom's mythic apple pie, public colleges are above reproach – a source of social mobility and economic productivity that we can hardly get too much of. Or maybe not. **Jeff Miron**, an economist at Boston University and a card-carrying libertarian, takes a critical look at the system and pokes some major holes in the conventional wisdom. "Even if one believes that public money should buy a college education for every high school graduate willing to put in the time," he writes, "it makes more sense to subsidize students at privately owned institutions."

KEN ORVIDAS

Millions of you didn't make it to this year's Milken Institute Global Conference in Los Angeles (your loss). So we thought we'd offer tantalizing bits of one of the highlights: **Michael Milken**'s roundtable discussion with Nobel-Prize winning economists **Gary Becker**, **James Heckman**, **Lawrence Klein** and **Douglass North**. Prepare for a few surprises.

Rounding out this thrill-packed issue, of course, are our regular features. The Charticle looks back at the stock market, **Bill Frey**'s Institute View analyzes the impact of demographic shifts on political power in the wake of the election. And last, but never least, our cartoonist **Mark Alan Stamaty** takes another swipe at the Washington establishment.

— Peter Passell

* *Actually,* The New Republic *magazine once ran a contest to pick the dullest* Times *OpEd headline. The winner, as I recall: "Promising Canadian Initiative."*

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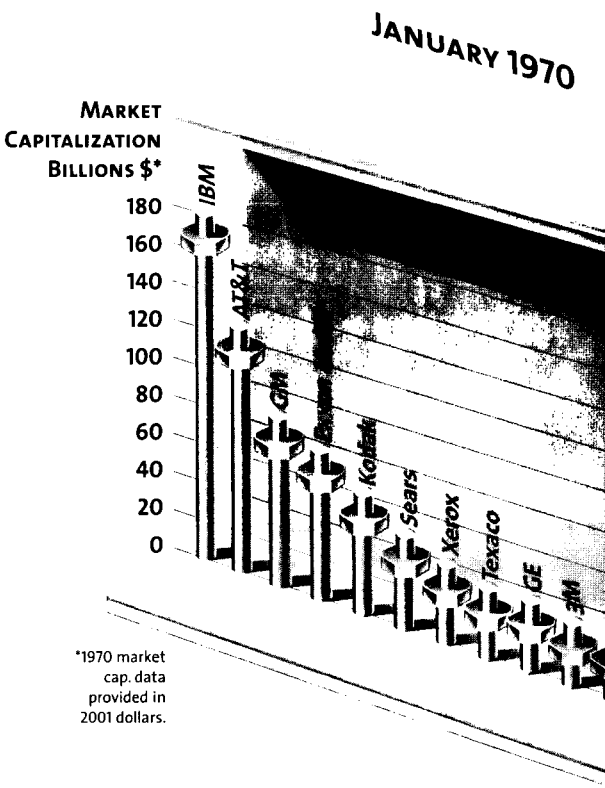
Hey, we know tech and phone stocks have really taken a beating in the last year. But step back a little, and you'll see how much the markets are still betting on the success of the New Economy. We've compared the top 20 corporations at the beginning of 1970, as measured by stock market capitalization, with the top 20 at the beginning of March 2001.

Back in 1970, Big Oil and heavy manufacturing (GM, Ford, 3M, DuPont) dominated the list. Thanks to our good buddies the Saudis, the oil patch has hung in there. But the auto and chemical companies are gone. Meanwhile, information technology (Microsoft, Intel, Cisco, IBM), drugs (Pfizer, Merck, Glaxo, J&J) and telecommunications (Vodafone, NTT, SBC, Verizon) have become towering presences.

That doesn't mean the economy has marched in lockstep. The securities markets reflect expectations more than they do realities. And while most of the growth of the last 30 years has been in what might loosely be called intellectual capital-based services, an awful lot of value-added is still in making stuff you can touch.

Perhaps the more profound insight to be extracted here is that Old Economy nuts-and-bolts businesses are so hemmed in by competition in global markets that nobody can make a killing. By contrast, New Economy industries are more likely to be in winner-take-most markets – places where being first and/or best with The Next Big Thing can be worth tens or even hundreds of billions of dollars.



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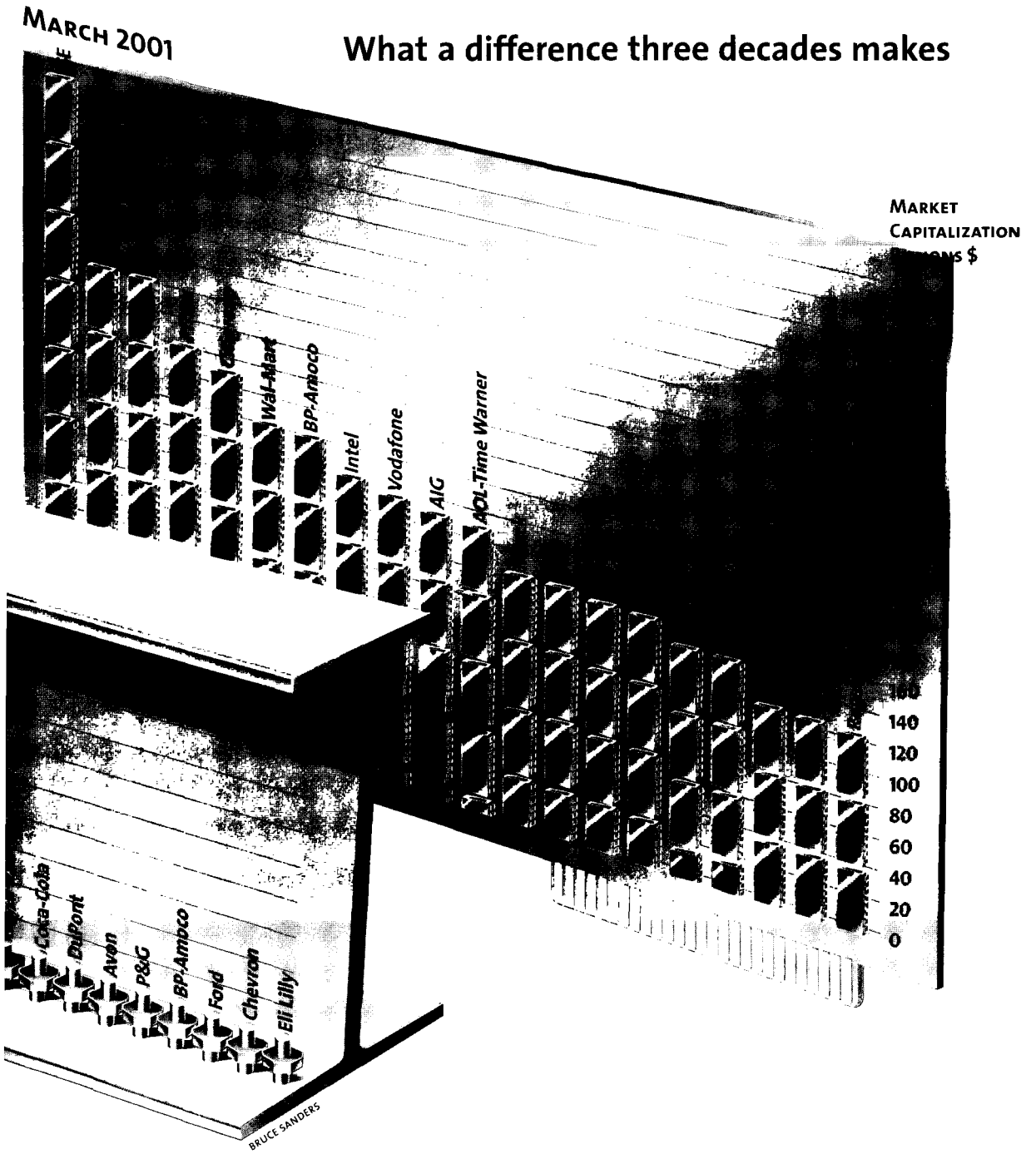

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BY ROB NORTON

The most startling feature of the economic policy debate during the presidential election of 2000 and of the current debate over the United States budget is the Democratic Party's unwavering support for sustaining the federal budget surplus.

From the July Democratic National Convention (when Al Gore beat back a series of attempts by the liberal wing of the party to call for increases in social spending and to de-emphasize fiscal restraint), through the ensuing election campaign (when Gore repeatedly warned against "squandering the surplus"), to today's debate over President Bush's plan to cut tax rates, the Democrats' primary domestic-policy aim is to preserve fiscal responsibility and future budget surpluses.

To say that the Democratic Party's position wasn't ever thus is to understate the case. The idea of balancing the budget – let alone running a surplus – is historically associated with the Republicans. Especially in the post-World War II decades, when Democratic policy making was influenced by Keynesian economists (and Republican policy making was informed by economists who were most easily described as anti-Keynesian), the idea that a balanced budget was inherently virtuous was seen as reactionary and anachronistic. Discretionary fiscal policy, in the postwar Keynesian view, held that budget deficits were generally acceptable, and should be used as a tool to boost federal spending to achieve the high-priority goal of full employment.

If anyone needed proof that balancing the budget was the wrong way to go, they were reminded of the last time the fiscal house was kept in order for an extended period of time: the prelude to the Great Depression, from 1921 to 1930. Indeed, the idea of balancing the budget was ridiculed by the ascendant generation of Keynesians as "Herbert Hoover economics."

So how did the Democratic Party morph from its traditional embrace of fiscal profligacy to its laser-like focus on budget balance, and how did the Republican Party lose its preeminent position as the party of rock-ribbed fiscal rectitude? Or as put more colorfully by Robert Reischauer, former director of the Congressional Budget Office and now president of the Urban Institute, how did we arrive at the current state of "policy cross-dressing?"

CROSS DRESSING REVEALED

There are at least three explanations. The first reflects a sea change in the views of academic economists. Through the 1960s, Keynesians ruled academia. Although the great English economist never directly recommended defi-

ROB NORTON, a freelance writer and columnist for *eCompany Now* magazine, is the former economics editor of *Fortune* magazine.

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cit finance as a tool of stabilization, his followers – notably Abba Lerner, the founder of the Keynesian theory of public finance – believed that government spending and taxation should be manipulated in the interest of maximizing employment rather than for producing a balanced budget per se. An important intermediate goal was to help the economy avoid recessions.

This Keynesian view reached its apogee of influence during the JFK administration, whose advisors included two future Noble laureates, James Tobin and Robert Solow. One tangible result was the cut of 1964, designed to increase output and lower unemployment by stimulating investment.

The Keynesian consensus came under profound attack in the early 1970s by the profoundly conservative school of "rational expectations." Its manifesto was a paper by the University of Chicago economist and future Nobelist Robert E. Lucas Jr., "Econometric Policy Evaluation: A Critique," which circulated in draft form for several years before its publication in 1976. The Lucas Critique, as it came to be known, argued that the static economic models upon which Keynesian policies relied were fatally flawed because they ignored the impact of policy changes on the way economic actors behaved.

The rational expectationists believed that once policy changes were announced, individuals and businesses would alter their saving and spending behavior in ways that offset the impact. A budget deficit, for example, would be seen as creating a debt that would have to be repaid down the road with an increase in taxes. As a result, much of the impact of countercyclical policy like tax-rate and interest-rate changes would be dissipated.

The Lucas Critique blew a giant hole in the theoretical foundations of Keynesian theory, and changed the way nearly all economists – including those disinclined to accept rational expectations as the new gospel – viewed macroeconomic policy. Its impact was especially great on those academic economists who came of age (and influence) during the mid-

1970s. These even included the group of rising young economists know as "New Keynesians," the most famous of whom was Lawrence Summers, who went on to become an economic advisor to the Democratic Party and later served as Treasury Secretary in the Clinton administration. (Summers was recently chosen to be the new president of Harvard University.)

The New Keynesians held to the basic beliefs of the old Keynesians – namely that the government should intervene in the economy, especially to avoid the kind of economy-

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wide market failures that lead to recessions. In light of the Lucas Critique, however, they had much more modest expectations of what government policy – especially fiscal policy – could accomplish.

Thinking in academia was also influenced by events in the 1960s and 1970s. The Kennedy tax cut, for instance, was formulated in the wake of the 1960 recession and formally proposed in 1962 – but didn't go into effect until 1964, when the economy was already well into recovery. When Lyndon Johnson sought to raise taxes to stop the inflationary spiral in 1966, the change proved to be too little, too late, and the boom was followed by a classic bust in 1970. The inability of government policy to prevent the recessions of 1970 and 1974, and the seeming inability of policy to cope with the frightening new phenomena of stagflation that characterized the 1970s, finished the job that the Lucas Critique had started: a chastened mainstream economics profession lost faith in the efficacy of countercyclical Keynesian fiscal policy.

THE REAGAN REVOLUTION

The second reason for the turnaround of the political parties' views on deficits, surpluses and the balanced budget was political, and was due to the influence of Ronald Reagan. While Reagan ran on a platform of balancing the budget and continued to call on Congress to cut spending throughout his presidency, his first priority was, in fact, to cut taxes. Close behind were his twin goals of increasing military spending and reducing discretionary domestic spending. With help from opportunistic Democrats he succeeded in pushing through a major tax cut – restraining the growth of federal revenues – and was successful in boosting military spending. But he was much less successful in cutting other spending. In addition, the back-to-back recessions of 1980-1982 had the effect of reducing tax receipts and increasing non-discretionary spending for things like unemployment insurance and welfare. The net result was budget deficits far larger than the United States had even seen in peacetime – deficits in the hundreds of billions of dollars that, in the memorable phrase of the budget director, David Stockman, appeared to stretch forward "as far as the eye can see."

The political effect was two-fold. First, by 1986, the budget deficit – $221 billion that year – was perceived as a crisis, bemoaned by economists, business leaders and politicians of every stripe, even eliciting criticism from international organizations and allied nations unaccustomed to lecturing Washington on matters economic. Controlling the deficit became a key concern of voters in both political parties. The matter-of-fact view of the average voter (which harkened back to the Republican view of the 1950s) was, "If I have to balance my budget, why shouldn't the government?" The groundswell of public disfavor led, among other things, to the passage of the Gramm-Rudman-Hollings Act, designed to force Congress to keep deficit spending down.

The other political effect was less obvious, but equally important. In the 1960s and 1970s, those who were in favor of balancing the budget – typically Republicans – were mainly concerned with cutting federal spending, especially the social welfare spending that had begun to grow so rapidly as a result of the Johnson and Nixon administrations' initiatives, such as enhanced welfare payments and food stamps. For Democrats, to oppose the balanced budget – to argue that deficits were a lesser evil – was to defend liberal social priorities.

But once Reagan made tax cutting his priority and the massive deficits of the 1980s

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were a reality, favoring the balanced budget could just as easily mean opposing the Reagan tax cut and favoring a return to higher pre-Reagan tax rates as a way to preserve federal spending. By the same token, opposing the balanced budget – or at least not actively seeking it – became, for some Republicans, a way of preserving low tax rates. Indeed, that policy stance was embraced by the new generation of Reagan Republican supply-siders.

Meanwhile, demographics were fundamentally changing the nature of the debate. Throughout the 1960s, as the giant baby boom generation entered the work force while the number of Americans reaching retirement age remained relatively small, there was little anxiety that government tax revenue would be inadequate to fund government spending. But in the 1980s, as the boomers reluctantly glimpsed the handwriting on the wall and the number of young people entering the work force dwindled, it became increasingly hard to ignore that by the early 21st century, the government would be hard-pressed to honor its promises to retirees.

Academic economists began examining the long-term effects of deficit finance, and a new consensus began to form that took the long view on fiscal policy. Reflecting the disfavor into which old-fashioned Keynesianism had fallen, there was now virtually no support for actively using deficit financing to stimulate the economy. New Keynesians and the conservatives influenced by rational-expectations theory converged on the view that keeping the budget in rough balance – perhaps even running surpluses when economic times were good – was good policy.

By the time the George Bush *pere* Administration took office in 1989, controlling the deficit was the number-one political priority – espoused, for different reasons, by politicians in both parties. Elite academics buttressed this conclusion. "The consensus is shifting," Lawrence Summers, then the youngest member of the Harvard faculty ever to be granted tenure, explained in 1990. Summers and his peers favored a balanced budget and a surplus in the Social Security accounts to reflect the need to reduce its actuarial deficit.

Edward Gramlich (then a public-finance economist at the University of Michigan and now a governor at the Federal Reserve Board) went further. "Something like three-quarters of the profession would support the goal of a surplus," he said.

The Bush budget for the 1991 fiscal year aimed for balance by 1993 and then to build surpluses throughout the 1990s earmarked for reducing the national debt. Bush's chief economist, Michael Boskin of Stanford, had no illusions that this would be an easy task. "It will take a lot of political acumen, as well as economic wisdom, to move in this direction," he said in early 1990. "But we think it is a tremendously important change."

Even though the idea of balancing the budget had become politically and economically respectable by 1990, Bush's plan to accumulate large budget surpluses still seemed unrealistic to many. "I don't believe it," said Charles L. Schultze, a Brookings Institution economist who had served in the Carter White House. "The Administration has been making promises to Congress for years, promising a balanced budget, but has never done anything." And the supply-side true believers made clear there would be a fight to get from here to there: an editorial in *The Wall Street Journal* in early 1990 sniffed that "envisioning budget surpluses requires a heroic suspension of disbelief."

Later that year, George Bush took a big step toward making his own projections come true by signing the Budget Enforcement Act of 1990, which included a tax increase. The

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law set the nation on a path toward fiscal responsibility. But when Bush lost the 1992 election to Bill Clinton, it seemed likely that policy again would stray from the path of fiscal righteousness. One of Clinton's first proposals after taking office in 1993 was a fiscal-stimulus package that included increased government spending designed to move the economy out of the recession that had started in 1990. (Ironically, it later became clear that the recession ended in 1991 and that the economy was well on the mend by the time the 1992 election took place.)

But Congress voted the stimulus package down, and Clinton, apprised of the fact that the recession was truly over, changed course by embracing the idea of balancing the budget. "Clinton basically wasn't trusted to be fiscally responsible," recalls Robert Reischauer. But his advisers – Alice Rivlin, Leon Panetta and Robert Rubin – convinced him that he had to impose a dose of fiscal restraint in the form of the 1993 budget act.

"At that point, the medicine began to work," says Reischauer. "The economy began to grow, the unemployment rate began to fall, and the rest is history. It was like sitting on a toboggan and enjoying the ride." Reischauer gives credit to the 1990 and 1993 budget acts, to the willingness of the Federal Reserve to maintain an accommodative monetary policy as the budgetary restraint took hold, and to pure dumb luck. "The three of those things coming together," he says, "produced a transformation of our fiscal situation that was nothing short of spectacular."

THE POLITICS OF SURPLUS

The next inflection point for fiscal policy – and the third factor in fiscal role reversal – came in 1997, when the total federal budget, including the Social Security accounts, moved into surplus. "The issue," explained William Gale, an economist at The Brookings Institution, "was whether the Clinton Administration would declare victory and take the surplus and spend it, or whether they'd hold out and go for an on-budget surplus. People like me wanted them to hold out, but it was unclear whether there would be the political will to do it. It turned out that the economy was so strong that it was easy."

There was also a question in 1997 whether the surplus would tempt the Republicans, who controlled Congress, to push for a tax cut. By standing firm for an on-budget surplus, the Clinton administration maintained the high ground in the debate, and headed off the Republicans' attempts to cut taxes.

The role reversal that had begun in the Reagan years was now complete: The Democrats were solidly behind the idea of a budget surplus because it had become the best way to protect government revenues. The Republicans were now against the idea of letting budget surpluses accumulate, because to do so forestalled the possibility of cutting taxes.

An editorial in *The New York Times* in 1999 noted that: "only a few years ago, the idea of Congress and the President wrangling over a trillion-dollar budget surplus would have provoked disbelief." But that's precisely where the policy debate wound up in the 2000 presidential election, and where it remains in 2001. The Bush administration has proposed a tax cut that would devote nearly all the surpluses over the next decade to reducing taxes. The Democrats, while bowing to the political fact that cutting taxes is always popular – and has special power right now due to the weakness of the United States economy – are seeking to preserve as much of the surplus as they can by limiting the size of the tax cut.

Who says political economy has to be dull – or predictable? M

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TO THE EDITOR:

As an eager young freshman a quarter century ago, I made the mistake of arguing for rent control against two economics majors. The gist of my argument was that the great demand for housing in Berkeley allowed landlords to charge unfair prices. This was met not with counter-arguments so much as with gales of derisive laughter. The gist of their hilarity was that the only coherent fair price is what buyers and sellers negotiate, and that even a naïve half-wit like me should see that any other way of setting prices is just capricious moralizing backed up by coercive government power. My earnest insistence that the city government really could calculate a fair return to landlords just increased their laughter and my frustration, as well as the amusement at neighboring cafeteria tables. It was my first encounter with the religion of economics, and though it did not keep me from later majoring in it myself, the memory has kept me ever wary of true believers.

I was quite surprised, then, to hear my freshman arguments echoed by Irwin Stelzer of the conservative Hudson Institute. Stelzer argues (Trends, First Quarter 2001) that the oil-producing nations are charging unfairly high prices. He complains that producers are "keeping the price of crude oil many times above the cost of finding, developing and producing new supplies." But how are we to secure this true and proper price, so far below what buyers and sellers have freely negotiated? By government intervention, of course! Despite twice invoking Reagan's policy "Don't just do something, stand there," and urging politicians "to add a liberal dose of laissez-faire to the policy mix," his argument brings him around to conclude, reluctantly, that we must have the government force oil producers into line with (coercive) trade policies and (dubious) legal action.

Stelzer's subversion of the central free market metaphor is perhaps the article's high point: "a more muscular version of the invisible hand would go a long way toward protecting consumers and the world economy." As if the muscular hand of government were a mere refinement of the invisible hand of the market! He nervously tries to avoid the inevitable consequences of this reasoning: "keep in mind, though, that if we get the price of oil right – including all costs associated with its use – there is little rationale for further government action."

Anyone following the argument will likely respond, "Huh? How d'you figure?" since traditional liberal rationales for government action – protecting the environment, promoting justice, helping the poor – are far better than Stelzer's rationale here. Like them or not, liberal principles do have a certain integrity. And like them or not, conservative principles do, too. The ultimate result of Stelzer scorning liberal principles while betraying conservative ones is a completely unprincipled policy supported by nothing but collective self-interest.

Jerry Cayford
Resources for the Future, Washington, D.C.
The opinions expressed are the author's, not his employer's.

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Changing the course

The Pill – the female oral contraceptive – turned 40 last year. It is a middle-aged medical miracle. Slimmed down to contain between one-tenth and one-twentieth the progestin, and one-third to one-sixth the estrogen of Enovid, the original birth-control pill, it remains the contraceptive of choice of American women. Some 44 percent of non-surgically contracepting women took The Pill in 1995, while 51 percent of those 15 to 24 years old used it as a contraceptive. Almost 80 percent of women now between 45 and 55 years old have taken The Pill at some point.

In its December 1999 millennial issue, *The Economist* chose The Pill as the greatest science and technology advance of the 20th century. It has been credited with the resur-

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By Claudia Goldin
and Lawrence F. Katz

The Pill and the Rise of women's education

gence of feminism in the 1960s, and the social and sexual revolutions of the 1970s. But no era of monumental social, political and economic change has a simple explanation. Major forces, with origins independent of The Pill, also had enormous impact on society in the late 1960s. The civil rights movement, for example, laid the foundations for the greater equality of women, while the war in Vietnam led to the expansion of the rights of youth.

Our goal, though less grand than explaining the upheavals of the late 1960s, is grand nonetheless: understanding a part of the mid-20th century democratization of American society. It concerns fundamental change in the lives of women, and how the aspi-

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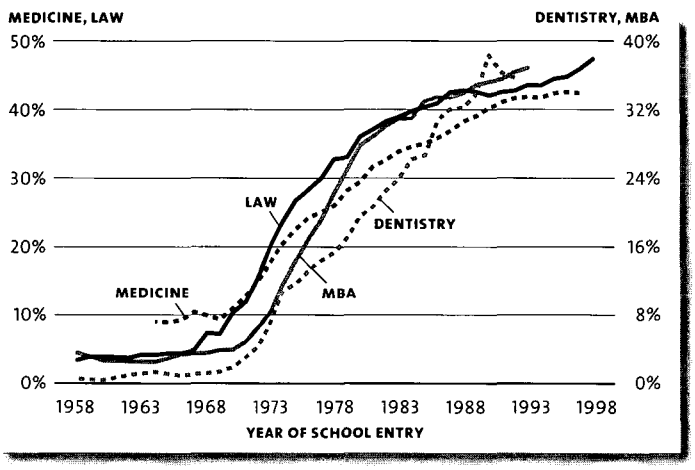
rations and career choices of young women were altered in the late 1960s. Real change in the economic and social status of women in the United States did not emanate simply from their increased participation in the paid labor force, for women have always worked. Rather, it came from their acceptance as equals in the most highly paid and demanding occupations – the professions.

PERCENTAGE OF FEMALE FIRST YEAR STUDENTS IN PROFESSIONAL PROGRAMS



A critical part of the change in women's economic status can been seen in the expansion in women's investment in professional careers. There was a sharp change around 1970 in the percentage of females among first-year students in medical, law, dentistry and MBA programs. Until around 1970, fewer than 10 percent of medical students were women, while the comparable figures for law (4 percent), dentistry (1 percent) and business (3 percent) were even lower.

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Just a decade later, the share was about one-third in medicine and business, more than one-third in law, and one-fifth in dentistry. And by the early 1990s, women represented more than 40 percent of all first-year medical and law students, and more than 35 percent of all first year MBA and dentistry students. Progress continues: according to *The New York Times*, women will outnumber men entering law school this fall. This increased flow of women into the professions, in turn, altered the total number of professionals who are women. In 1999, 27 percent of all physicians were women, while 29 percent of all lawyers and judges were women.

Did The Pill play a role in this decision by millions of women to invest in professional training and pursue careers? We think the answer is a resounding "yes." Beginning in the late 1960s, safe, reliable, easy-to-use, female-controlled contraception enhanced the ability and willingness of young women to enter careers that involved extensive, upfront time commitments to education.

A college woman contemplating a lengthy professional education had to consider all of the costs of the investment. In addition to the financial costs of education and forgone income, she also had to evaluate its social consequences. If she did not marry before her professional education began and lacked an almost foolproof contraceptive such as The Pill, she would have to pay the penalty of abstinence or cope with uncertainty regarding pregnancy. If she delayed marriage while training for her career (as many did, relative to all college-graduate women), she would also have to consider the social consequences

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of a depleted marriage market.

The Pill thus enabled a larger group of women to invest in expensive, long-duration training without paying a high social price. It accomplished this feat through a least two routes. First and most obvious, The Pill is a highly reliable form of contraception that allows women to engage in sexual relations without having to worry about unintended pregnancies that could disrupt career plans. We consider this impact to be The Pill's *direct* effect.

The increased certainty regarding pregnancy that was gained from using The Pill need not have been enormously large to have had a great impact. But The Pill, particularly in its early high-dose incarnation, was monumentally more reliable than were other methods of contraception, especially so for the sexually inexperienced. The diaphragm has seven times the failure rate in typical use, while the condom has four times the failure rate.

The Pill also had an *indirect* effect on women by encouraging an increase in the age at first marriage. A woman with a law degree who decides to marry at age 27, rather than just after college, may discover that the marriage market is rather thin if the age at first marriage among college graduates is low. But if the marriage age for graduates rises, as it

CHARLES GATEWOOD/THE IMAGE WORKS

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did throughout the 1970s, the delay in marriage would involve far less of a penalty.

To put it another way, The Pill lowered the cost of pursuing a career through its direct effect on the cost of having sex and its indirect effect of increasing the age at first marriage generally. Note that even women who were never on The Pill benefited from its existence if they wanted to delay marriage to invest in long-duration training: by enabling marriage delay, The Pill created a thicker marriage market for those wanting to marry after investing in a professional education.

The Pill had additional impact through other routes, which we do not directly examine. For example, it allowed the mentors of young women to be more secure in their belief that their female students, as undergraduates or in professional schools, would be able to control their fertility and not drop out to raise a family. By the same token, larger networks of female students may have made attending professional school more attractive for women.

Our challenge is two-fold. We must empirically locate the connection between The Pill and young women's careers in the early 1970s, and we must also confront why there was a lag of almost 10 years from the date of The Pill's availability as a contraceptive to the start of the career response.

CHARLES BONNAY/TIMEPIX

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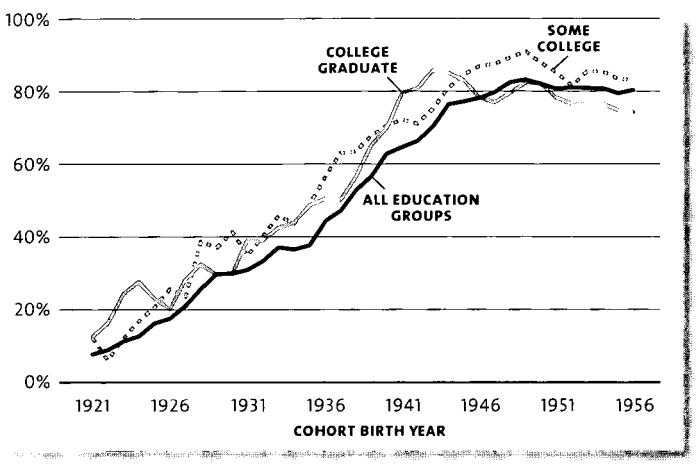
The explanation for the latter is simple: single women in the 1960s were thwarted from obtaining The Pill for contraceptive use by archaic state laws. As those laws were relaxed, young women were able to obtain The Pill and, subsequently, the marriage age rose and career aspirations changed.

But isolating the impact of The Pill from other factors affecting the rise of women in the professions is more difficult. Some of our evidence consists of coincident turning points in various time series for Pill use by young women and the entry of women into professional programs. Reinforcing and convincing evidence is derived from the fact that there was considerable variation in state laws and judicial decisions that enabled young women to obtain The Pill – and that these laws affected the use of The Pill by young women and, in consequence, the age at first marriage among the college-educated.

PERCENTAGE OF WOMEN EVER TAKING THE PILL, BY EDUCATION (THREE-YEAR CENTERED MOVING AVERAGE)



A POPULAR DRUG WITH A DIFFICULT BIRTH

The road to an effective oral contraceptive involved scientific discoveries in physiology, completed in 1937 with the discovery of the role of progesterone in ovulation, and the synthesis of sex hormones. All sex hormones nest chemically in the class of steroid compounds, and the synthesis of one steroid, cortisone, in 1949 opened the way to the invention of synthetic progesterone (norethindrone was the first) in 1951. But the pharmaceutical companies were not fully committed to contraceptive research and developed synthetic hormones as therapeutics, not as a means of birth control. Cortisone, used to relieve the symptoms of arthritis, was accurately forecast to be a highly profitable drug. Oral contraceptives, on the other hand, posed potential problems for drug makers in a country that still retained Victorian legislation at the state level and was about one-quarter Catholic.

Although the pharmaceutical makers employed scientists to work on synthetic sex hormones, they did not allocate much money to oral contraceptive research. In fact, research on The Pill was largely bankrolled by a wealthy philanthropist with no financial connection to the pharmaceutical industry. The philanthropist, Katherine Dexter McCormick, an admirer and friend of the tireless birth control pioneer Margaret Sanger, was persuaded by Sanger to fund part of the project. Thus it is said of The Pill that it had four fathers (Frank Colton and Carl Djerassi, who synthesized progesterone, and pill researchers Gregory Pincus and John Rock) and two mothers.

The 1956 human drug trials on the oral contraceptive were held in Puerto Rico, far from the prying eyes of potential opponents.

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The FDA gave Searle approval for Enovid for medical use in 1957 and for contraceptive use in 1960; by 1964, four pharmaceutical companies were marketing a version.

The Pill was an overnight success, even among Catholic women. It diffused rapidly through its target population of married women. Indeed, the fraction of married women (under age 35) who were on The Pill came close to its historic maximum just five years after its release.

But it was not so successful among young single women for another decade. Contemporaneous data reveal that the fraction of 18-year-old, never-married women who had ever taken The Pill was 10 percent in 1971, but 27 percent in 1976 (28 percent and 56 percent respectively for those who were not virgins). The portion of married women taking The Pill had already peaked by the mid-1960s, but the numbers for unmarried women continued to rise to the mid-1970s. The reasons for the delay were both legal and social.

Unmarried women did not begin to take The Pill in large numbers until the late 1960s and early 1970s, when almost all states lowered the age of legal majority and granted youth the rights of adults through "mature minor" decisions. Those legal changes were not driven by legislators' or courts' desires to extend family-planning services. Rather, they were motivated by factors similar to those that led to the ratification of the 26th Amendment (which lowered the voting age to 18) in 1971. The Vietnam War awakened Americans to the inconsistency between the rights and responsibilities of young people, and they chose to extend greater rights to them.

We emphasize the changing circumstances of young, unmarried women because their altered perceptions of marriage and fertility enabled them to plan lives that were different from those of previous generations, and to do so early in their personal development. A disproportionate number of women in professional education programs, moreover, were (and still are) unmarried.

The point is that the reliability and general safety of The Pill enable women to better plan for careers at an early stage and be taken more seriously by mentors, schools and employers.

A brief digression is in order here to understand the constraints on women in broader context. The social and legal climate of the mid-20th century United States was influenced by the remnants of the late 19th century era of Comstockery regarding contraception and obscenity. The 1873 Comstock Law, named after its champion, the anti-vice crusader Anthony Comstock, made the importation and mail shipment of all forms of contraceptive devices and information a federal crime. The law was never very important and was effectively modified by judicial action in 1936 to allow the importation of contraceptives. Its real legacy was in state Comstock laws that had considerably more impact both on commerce in contraceptives and on freedom to use them.

As late as 1960, 30 states prohibited advertisements regarding birth control devices and

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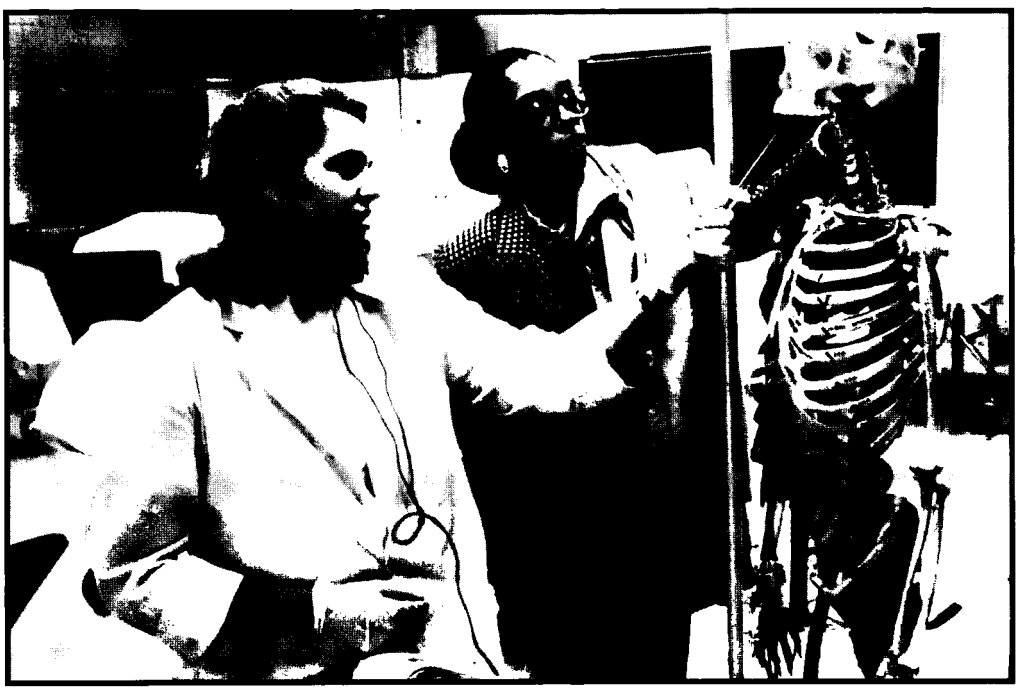
22 had some prohibition on the sale of contraceptives. One of those laws was struck down by the United States Supreme Court in *Griswold v. Connecticut* (1965), which affirmed the right of married couples to use contraceptives in the privacy of their bedrooms. The last surviving remnant was reversed by



TARO YAMASAKI/TIMEPIX

another Supreme Court decision, *Eisenstadt v. Baird* (1972), which overturned a Massachusetts law prohibiting the sale of contraceptives to unmarried people. Although many of the Comstock laws were easily circumvented by married individuals, they had an important effect on minors, whose ability to obtain contraceptives was also limited by social norms. You don't have to be very old to remember tales of embarrassing confrontations between teenage boys and their unfriendly neighborhood druggists.

SEX, THE PILL AND SINGLE WOMEN

Unless a state recognized the mature minor doctrine by law or judicial interpretation, parental consent was legally required for a minor to obtain birth control devices, prescriptions and related information. A minor could be emancipated in various other ways, including marriage, and physicians sometimes used their own judgment in these matters – although local norms often constrained and guided their decisions. College health services, however, paid more attention to the laws of their states, and few, if any, college health clinics made family planning services available to students before the 1970s.

With sufficient ingenuity, a determined young, unmarried woman presumably could obtain The Pill without benefit of enabling laws. But our cross-state statistical analysis for the year 1971 shows that Pill use among young women was considerably higher in states with lenient laws regarding the rights of minors.

The rights of minors began to expand

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slowly in the 1960s, and then far more rapidly in the early 1970s with the reduction of the voting age to 18. The age of majority was less than 20 for women in just seven states in 1969. By 1971, this number had expanded to 18, and by 1974, 43 states set the age of majority below age 20.

In 1969, only three states had laws enabling a female younger than age 17 to obtain contraceptives; such laws existed in 12 states in 1971 and in 27 states in 1974. It should be noted that those laws only inadvertently applied to contraceptives. They either lowered the age of majority, which enabled youths to engage in transactions such as signing rental contracts, or they applied to a wide range of health services such as surgery, without parental consent.

The same forces that prevented young, unmarried women from obtaining The Pill in the 1960s hinder today's social scientists from studying those women's use of contraceptives. There are no contemporaneous surveys of Pill usage by young women in the 1960s, while just two exist for the 1970s – and they are of limited value.

To measure trends in Pill usage we employ, instead, two retrospective surveys from the 1980s. But these have drawbacks as well. Most important, the survey that gives direct information on Pill usage does not contain information on the age at first marriage. The second survey contains marriage age and the age at which family-planning services (of which obtaining The Pill is the most important) were first obtained.

We have also used data on the take-up rate of The Pill for females 15 to 19 years old in 1971 and 1976. All of these series, taken together, show that the diffusion of The Pill among young unmarried women began more than five years after it did for married women, and that it reached its highest levels among this group considerably later. They also show that Pill usage among single, college-graduate women began to soar with cohorts born around 1948.

The figure on the next page illustrates the trend, showing the percentage of women receiving their first family planning visit among those who eventually graduated from college and were not married by age 22. These data may slightly overestimate the fraction obtaining The Pill, since family planning visits were also used by those seeking other services, such as pregnancy counseling. Nevertheless, the data are fully consistent with other information on Pill usage and clearly show that the fraction of young, unmarried, college-graduate women obtaining family planning services greatly increased with those born in the late 1940s. These were precisely the women who first began to enter professional schools around 1970.

CAREERS, MARRIAGE AND THE PILL

The timing of the changes in the fraction of females among first-year professional students and the diffusion of The Pill could, of course, have been a coincidence. But we have additional evidence that suggests the relationship is causal.

First, as previously noted, young unmarried women in states that lowered the age of majority or had passed legislation extending the mature minor decision (or had judicial rulings that did so), were considerably more likely to use The Pill. Second, the age at first marriage increased for college-graduate women who turned 18 around the time that the state laws changed. That is, the availability of The Pill to young college women appears to have led to an increase in the age of first marriage, as identified in a cross-state analysis that includes controls for year of birth and

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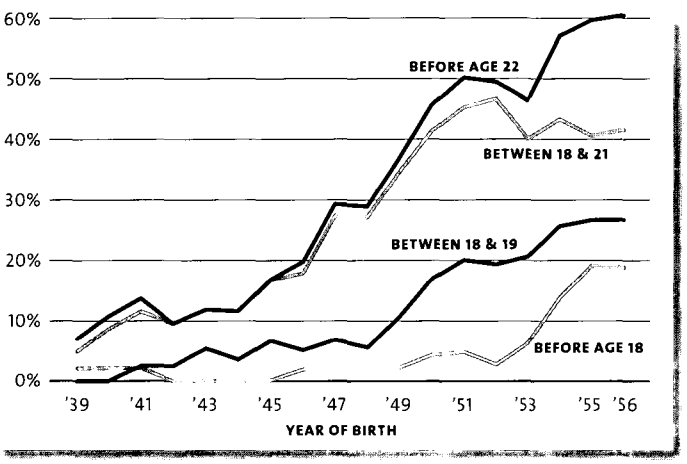
state of birth, as well as state time trends. The Pill encouraged the delay of marriage through several routes – for example, by reducing the necessity to become engaged or marry in order to have sex without the risk of scandal, and by lowering the incidence of shotgun weddings.

The increased age at first marriage among college-graduate women is striking. Among women born from the early 1930s to the end of the 1940s, about 50 percent married before age 23. That is, half of all women who completed college married within a year or two of graduation. But among women born in 1957, only 30 percent married before age 23. The age at first marriage increased greatly between cohorts born in 1950 to 1957, and in those intervening seven years, The Pill greatly diffused among young, unmarried college women.

PERCENTAGE OF (UNMARRIED) COLLEGE-GRADUATE WOMEN RECEIVING FAMILY PLANNING SERVICES



WAS IT ONLY THE PILL?

The case for The Pill as the primary factor driving women's career decisions is strong. But it is not the only possible factor. There is also abortion, legalized nationwide in 1973 by the Supreme Court and permitted earlier than that by several states. We have found, however, that abortion was not as potent a factor as The Pill in encouraging later marriage for college women, although its impact on careers probably complemented that of The Pill.

Fertility reduction and later marriage ages do not require the widespread availability of a safe, reliable contraceptive. In the United States, fertility declined secularly and the marriage age rose during the 19th century, long before the diffusion of modern contraceptive methods. The Pill was legalized in Japan in 1999 (!!), but fertility is very low and the marriage age rose considerably in the 1970s and 1980s. The Japanese case, however, may prove the rule: there has been very little real social change in the lives of Japanese women. The point is that the reliability and general safety of The Pill enable women to better plan for careers at an early stage and be taken more seriously by mentors, schools and employers.

Young American women in the late 1960s had hoped to follow in their mothers' footsteps, but in just a few years their aspirations had changed radically. How much of this change was due to the resurgence of feminism, general social change, and the legacy of the civil rights movement, all reinforced later with policy changes such as affirmative action, and how much was due to The Pill? There is considerable evidence that The Pill had a large effect on career and marriage. Without The Pill, these changes would, presumably, have come later. How much later, though, we do not know. M

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Supply and

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An economist goes to

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AP/WIDE WORLD PHOTO

The hardest ticket to get this year was for Super Bowl XXXV. Though the game proved to be a blowout, thousands of fans who were desperately seeking a seat to the spectacle were shut out. One can learn a lot about economics from studying the distribution and pricing of Super Bowl tickets. Herewith, my reports on what I learned from taking my father, Norman, to the game and conducting an informal survey of 316 fans with the aid of four interviewers.

The most obvious fact about Super Bowl XXXV was that the price listed on the tickets – either $325 or $400, depending on the section of the stadium – was well below the figure that would have balanced demand with the fixed supply of seats in Raymond James Stadium in Tampa. As a consequence, there was tremendous excess demand. The National Football League held a lottery for the rights to purchase 500 pairs of tickets so ordinary fans would have a shot at going to the game, and it was inundated with 36,000 applications. (The odds of being admitted to Princeton are a lot better.) On game day, at least 1,000 frustrated fans displayed "ticket wanted!" signs outside the stadium, and ticket holders told stories of being offered as much as $5,000 as they ran the gauntlet.

List prices were set by the NFL commissioner's office in conjunction with the Super Bowl Policy Committee, which consists of a handful of team owners. Tickets were rationed as follows: The league kept 25 percent, distributing them to the media, advertisers and others. The two teams got 17.5 percent of tickets each, most of which they distributed to their season-ticket holders through lotteries. The host city got 8.35 percent of tickets, and the other teams in the league divided what was left.

Roughly three out of four states and many municipalities regulate the resale of tickets. Nonetheless, a secondary market for Super Bowl tickets operated by scalpers, licensed ticket brokers and online auctions quickly sprang up. A week before the Super Bowl, tickets on Yahoo! Auctions, for example, traded for $1,500 to $3,500. Although the Tampa police aggressively discouraged scalping, the prohibition was easily skirted. For example, someone in a state that outlaws the resale

the Super Bowl

By Alan B. Krueger

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of tickets can still purchase a ticket from a broker in a state that allows resales because the states cannot regulate interstate commerce. In addition, although eBay eventually requested that all tickets posted without accompanying amenities be withdrawn, it still permitted auctions for tickets that had been packaged with something else – a hotel stay or a plane ticket.

To economists, scalping is a benign activity that creates value. Those who voluntarily buy and sell tickets do so only because they feel they will benefit from the transactions. Football fans seem to agree with the dismal scientists. Two-thirds of the 316 fans we surveyed thought ticket scalping should be legal. And a slightly higher percentage among those who obtained their tickets (at list price) through a team lottery agreed.

Driving market transactions underground can be quite inefficient. First, there is greater risk of counterfeiting. Second, transaction costs rise, although many transactions still take place. And third, tax revenue is forsaken, as scalpers are unlikely to pay taxes.

Although the "law of one price" tells us that in a competitive market identical goods should sell for the same price, Super Bowl tickets varied widely in the secondary market. Even tickets sold in auctions on the Internet on the same day went for different prices. This phenomenon has been observed in many markets, so I doubt it is due to anti-scalping legislation. Nonetheless, except in markets for goods with regulated prices, I think it is fair to say the law of one price has been repealed by experience. I call the replacement, Card's Law of Infinite Prices, after the University of California economist David Card, who showed that all Boeing 747 pilots were paid the same salary when airlines were regulated and then were paid widely varying salaries after deregulation.

The NFL itself auctioned two pairs of Super Bowl XXXV tickets on eBay, as part of a VIP package that included five or six days of wining and dining in Tampa, an invitation to the half-time show rehearsals, and meetings with players and coaches. One package went for $22,500 and the other for $17,100!

There is even evidence that prices vary systematically in auctions for less extravagant items. For example, my Princeton colleague Orley Ashenfelter found that identical lots of wine tend to sell for lower prices in later rounds of an auction. Similar price movements have been identified in auctions for condominiums and artwork. This pattern has been dubbed "the declining price anomaly."

At the Super Bowl, however, prices did not decline as the kickoff approached. Indeed, the supply of tickets all but dried up a few days before the game. I would estimate that thousands of fans were stranded outside the gates, even though they were willing to pay substantially more than many of those seated inside. There was thus a declining supply anomaly, not a declining price anomaly. The fear of this happening might explain why prices typically decline in later rounds of auctions; those who want something the most buy early in case it won't be available later – and pay a premium to avoid the risk.

In view of the predictable excess demand, it is natural to ask why the NFL doesn't charge more. Although the face value of Super Bowl tickets has increased, almost quadrupling since 1987, tickets on the secondary market still sold for $1,000 to $4,000 more than list. By charging a market price for tickets – say, an

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average of $2,300 – the NFL could have increased its revenue by some $150 million.

That's a lot of money to leave on the table. By contrast, the television ad revenue generated from the game was $200 million.

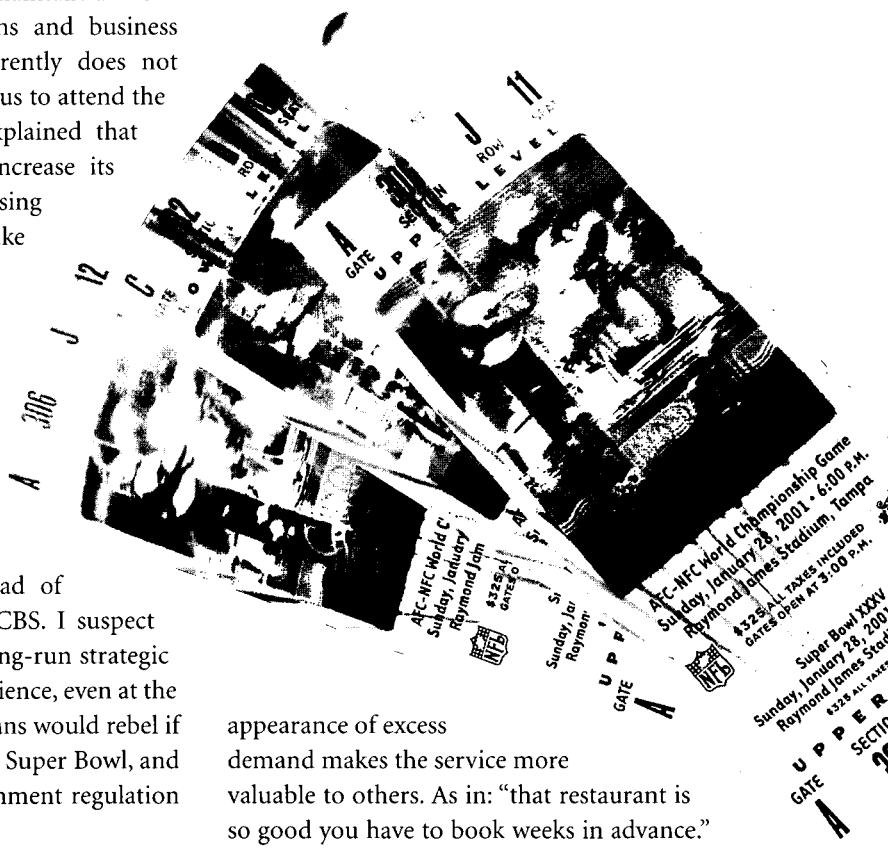
So why doesn't the NFL charge more? I put the question to Greg Aiello, the NFL's vice president for public relations. He explained that the league tries to set "a fair, reasonable price" because it wants to maintain an "ongoing relationship with fans and business associates." The NFL apparently does not want only the rich and famous to attend the Super Bowl. He further explained that although the NFL could increase its "present-day profit" by raising ticket prices, it prefers to take "a long-term strategic view."

A related phenomenon concerns television rights. With almost one billion viewers worldwide, the NFL could surely raise more revenue by selling television access to the Super Bowl on pay-per-view, like prizefights, instead of selling broadcast rights to CBS. I suspect the league feels it is in its long-run strategic interest to attract a wide audience, even at the cost of short-term profits. Fans would rebel if they had to pay to watch the Super Bowl, and the league might fear government regulation if it restricted TV access.

The explanation the NFL gives for setting the price of Super Bowl tickets below what the market will bear seems consistent with a model proposed by the economist David J. Salant almost a decade ago. Salant argued that professional sports teams have an implicit long-term contract with their season-ticket holders. The fans agree to support the team in lean years, and the team agrees to treat loyal fans fairly. Thus, the spot market price is not the relevant price in this market.

Nobel Prize winner Gary Becker's innovative model of restaurant pricing offers an alternative interpretation. Becker argues that restaurants (and sports teams) sometimes fail to raise prices despite long queues because the appearance of excess demand makes the service more valuable to others. As in: "that restaurant is so good you have to book weeks in advance." If this is indeed the case, restaurants and sports teams can maximize profit by rationing access. I suspect the Salant fairness model provides a better description of Super Bowl ticket pricing in view of the NFL's explanation of its behavior and the way it treats season-ticket holders.

Nonetheless, the NFL's behavior raises serious questions from the standpoint of con-



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ventional economics. Wouldn't it be more efficient for the NFL to sell tickets at market value and give season ticket holders and business associates some of the extra cash? Moreover, one would expect that allocating tickets in a lottery at a below-market price would not determine who is in the stands – those who want tickets the most and have the wherewithal would buy them from lottery winners.

In fact, the NFL seems to know what it's doing. According to our survey, 28 percent of fans attending the game received tickets in a lottery, and another 11 percent received them from the NFL. Forty percent of attendees received tickets as gifts for which they paid nothing in 85 percent of these instances and just the face value in 14 percent.

Only 20 percent of attendees paid more than face value for their tickets. This finding raises an interesting question: since the effective supply of Super Bowl tickets to the market may have been only 15,000 or so, maybe the market value of a ticket if the entire stadium were on the auction block would be substantially less than the prices attained in the secondary market. Although we cannot estimate this hypothetical price, I suspect that the stadium would still have sold out if the NFL had raised the face value of Super Bowl tickets to $1,500. As explained below, a force greater than rational economic self-interest might explain the limited resale market for Super Bowl tickets even at exorbitant prices.

Ninety-two percent thought it would not "be fair for the NFL to raise the face value to $1,500 if that is still less than the amount most people are willing to pay for tickets." Even among those who paid more than $1,500 for their own ticket, 83 percent still thought it would be unfair for the NFL to charge more than $1,500! Evidently, belief in free markets is the first casualty when it comes to Super Bowl tickets.

The finding that fans consider it unfair to raise prices in response to excess demand should not come as a surprise in view of a pair of papers published in the *American Economic Review*, one by by Daniel Kahneman, Jack Knetsch and Richard Thaler, the other by Robert Shiller, Maxim Boycko and Vladimir Korobov. The first trio of researchers found that people consider it unfair for businesses to raise prices in response to excess demand (for example, it is considered unfair to raise the price of shovels after a blizzard) or to monopoly power, but it is fair to raise prices in response to an increase in costs.

The second trio found that Muscovites and New Yorkers had essentially the same perceptions of what constituted fair business dealings in 1990. For example, in both cities, two-thirds of the respondents thought it was unfair for flower shops to raise prices on holidays, when there is great demand for flowers.

The NFL has more reason to worry about perceived fairness than most businesses. Over the course of a season, 60 percent of the NFL's $4 billion in revenue comes from TV. So maintaining a positive relationship with fans and advertisers is important, and arguably worth the sacrifice of short-term profits. Drastically higher ticket prices would undoubtedly hurt the NFL's image.

If fans acted like rational economic agents, then fairness considerations wouldn't matter and the tickets would end up in the hands of those willing to pay the most for them. One thing we learned from our survey, though, is that rationality was in short supply at the Super Bowl. We asked fans who had won the right to buy a pair of tickets for $325 or $400 each in a lottery whether they would have been willing to pay $3,000 a ticket if they had lost in the lottery and whether they would have sold their tickets if someone had offered

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The Super Bowl Fan Survey

The survey described in the article was conducted by four professional survey interviewers from Tampa FL, and designed by Alan Krueger with the assistance of the Princeton University Survey Research Center. The four interviewers arrived at the stadium shortly after noon on game day and asked fans in a catch-as-catch-can fashion whether they would answer eight short questions. They continued working until around 6 pm; kickoff time was at 6:25 pm and most fans filed into the stadium before then to hear Ray Charles sing "America the Beautiful."

A total of 316 fans were interviewed; hardly anyone who was asked refused to be interviewed. Indeed, tailgating fans seemed eager to tell their stories of how they got to the game. The survey participants were not a representative sample of Super Bowl attendees, however. For example, fans who arrived early were more likely to be interviewed. Nevertheless, it is unclear in which direction, if any, the non-random sampling design might affect the results.

To warm up the respondents, the first two questions on the questionnaire were: "Which team do you want to win?" and "Which team do you think will win?" The answers to these questions, cross-tabulated below, are interesting in their own right. By and large, football fans expect that the team they want to win will win. To the author's regret, more Ravens fans than Giants fans were right.

NUMBER OF RESPONDENTS WHO:

		Expect to Win			
		Giants	Ravens	Don't know	TOTAL
Want to Win	Giants	148	7	6	161
	Ravens	13	109	3	125
	Don't care	9	16	5	30
	TOTAL	170	132	14	316

them $3,000 apiece. (The order of these two questions was randomly changed on the questionnaire.) Ninety-four percent said they would not have bought for $3,000, and 92 percent said they would not have sold at that price. Fully 86 percent answered "no" to both questions, seemingly unconcerned by the contradiction. (When the willingness to sell question was asked first, 93 percent answered no to both questions; if the willingness to buy question came first, 80 percent answered no to both questions.)

It is, of course, possible that the fans who had already showed up at the game were more reluctant to sell than the larger population; that is, our results could have been affected by selection bias. Moreover, the fans at the game might have been more willing to sell if they had been offered $3,000 per ticket before booking their airplane and hotel reservations and traveling to Tampa, or if they had been given genuine offers of cash at the game instead of a hypothetical question from an interviewer. But researchers have documented a significant divergence (about 2:1) between the price at which individuals are will-

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ing to sell and willing to buy other items in experimental settings, so this finding is probably not an artifact of my survey. Richard Thaler of the University of Chicago calls this an "endowment effect," because the value people place on a good increases once it is added to their possessions.

The endowment effect helps explain how the NFL can influence who goes to the Super Bowl by distributing tickets in a lottery, and why there was apparently such a small resale market for tickets.

The existence of the endowment effect raises three important, interrelated issues for economics. First, markets may be missing, or "too thin," because people are (irrationally?) reluctant to part with their possessions. Second, if the price at which an individual is willing to accept or sell an item is different, it is unclear how prices should be used in traditional cost-benefit analysis commonly used in public policy decisions. Which value really makes sense, the minimum selling price or the maximum buying price? Third, and most profound, the endowment effect poses a challenge to a fundamental theorem underlying modern economics – namely, after free markets work their magic, no one can be made better off without making someone else worse off.

But if the endowment effect induces people to overvalue what is already in their possession, then the voluntary trades that produce this "Pareto optimal" distribution may not take place. Conceptually, at least, it might be possible to rearrange goods so some individuals' welfare rises without causing anyone else's to fall. It is far from clear, however, whether such Pareto-improving transfers could be made in practice.

A further fly in the ointment for any policy decision based on the endowment effect is that it does not apply to everyone. Before the kickoff, I asked Karen McClearn, an exuberant Ravens season-ticket holder from Baltimore seated next to my father, whether she would have sold the ticket that she and her husband obtained in the lottery for $325 if someone had offered her $4,000 for it. She said no. She added she might have been willing to pay up to $5,000 for a ticket if she had not been selected in the lottery. Her husband, Richard, interjected the obvious fact that this was why they would not have sold their tickets for $4,000.

But when the Ravens took a 17-0 lead – and Karen concluded her rendition of the Ravens' bird dance, which almost inadvertently knocked my dad out – she volunteered that she would have been willing to pay $1 million for her ticket.

Although football fans are subject to psychological biases in judgment, they apparently don't let emotion cloud their minds when it comes to taking account of tax rules. Some of the tickets sold on eBay and Yahoo! were auctioned on behalf of charities, which makes the purchase price above the face value tax-deductible for the buyer. In these cases, tickets sold for a premium. For example, two upper-level seats auctioned for the Boomer Esiason Foundation to help fight cystic fibrosis sold for $7,300, which amounts to an after-tax price of $4,667 at the top marginal tax rate of 39.6 percent – quite close to the typical price for a comparable pair of tickets in the secondary market.

Overall, I have become persuaded that Berkeley economist George Akerlof's "gift exchange" model has much to offer in understanding how the market for Super Bowl tickets really works. Akerlof's view is that transactions in some markets involve a gift exchange motive. Employees work harder if they feel they are treated fairly; they exchange

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the gift of high effort in exchange for the gift of fair pay. Within limits, social norms determine the fair price.

I suspect the gift exchange motive explains how most fans ultimately get to the Super Bowl. It is socially unacceptable to resell a present to the highest bidder – at least if the person who gave the present might find out that it was resold. Also, if you do accept payment for a gift, it is socially unacceptable to charge a friend more than you paid for the item, which is why an overwhelming majority of those who received tickets as gifts paid nothing at all or face value for them.

Indeed, even after the game the clash between the gift and transactions exchange motive of Super Bowl tickets continued. Several people offered to pay $10 for my ticket stub as we exited the stadium. When I said no, the price jumped to $20. But I wouldn't sell: I planned to give the stub to my children. I didn't see many others in the exiting crowd selling their ticket stubs, either.

The ticket stub market, incidentally, may be a highly profitable one. While writing this paragraph, I tapped into eBay to see how much stubs were selling for. The bidding was between $52 and $71 for Super Bowl XXXV ticket stubs in mint condition. For reasons only a true collector could understand, stubs for seats located in better sections of the stadium were selling for more.

I suspect that the gift exchange and the thinness of markets is one reason the Super Bowl, and sporting events more generally, are so appealing to businesses. Many bring their clients to games to schmooze with them to make deals, or give their clients tickets to win them over. How else could one justify business expenses on luxury boxes? Indeed, even the NFL itself says it retains a sizable share of Super Bowl tickets to maintain good relations with its business associates. From a narrow economic standpoint, it would make more sense to add some of the money spent on these endeavors to the economic transactions and retain some as profits.

I shall conclude with a modest proposal. The NFL has good reason to eschew short-run market forces in setting Super Bowl ticket prices. Nonetheless, the current method for allocating tickets is highly inefficient. Tickets do not always go to those who value them most highly, a great deal of time and energy is wasted searching for tickets, taxes are evaded, and people who buy tickets from scalpers run the risk of receiving a counterfeit ticket and of being arrested.

So let's change the rules. The NFL should set aside 5,000 tickets scattered through the stadium to sell in an open, online auction for whatever price the market will bear. The proceeds of this auction, above the face value of the tickets, should be donated to charity. For example, the NFL could use the proceeds to take inner-city kids to games during the regular season. The NFL auction should be held shortly after the AFC and NFC championship games, so that fans would know whether their favorite teams will play and would have enough time to make travel plans.

This proposal would seem to have several advantages over the current system. First, those who really want to attend the game would be able to attend, at a market-determined price. Second, the charity that receives the proceeds would obviously benefit, and the NFL would also benefit from the resulting goodwill. Third, the auction would establish a market price for legitimate tickets throughout the stadium; scalpers would find it difficult to charge more than the price obtained in this open auction. Fourth, buyers would be confident that the tickets they purchase are not counterfeit.

Next problem, please. M

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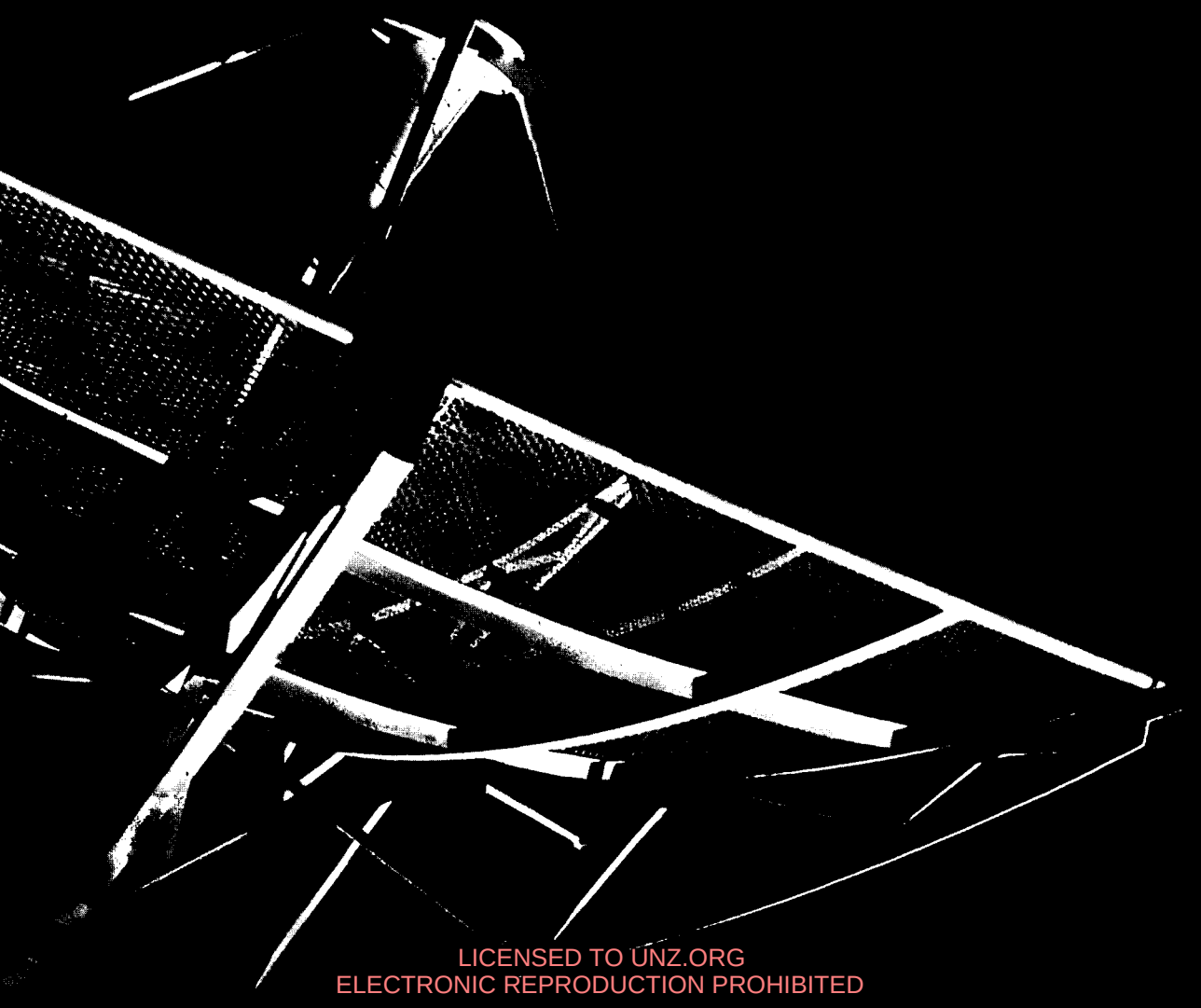
SPEC



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TRUM For Sale

By Lawrence J. White

The electromagnetic spectrum can't be seen, tasted, touched or smelled – though a few zillionaires like Craig McCaw, Ted Turner and Sumner Redstone apparently detected the faint scent of money some years ago. Nor is the spectrum high on most people's lists of pressing concerns. But its use will strongly influence the direction and impact of modern telecommunications technology – notably the "broadband revolution" of information dissemination and retrieval that has the potential to change (well, almost) everything.

Unfortunately, spectrum use is mired in layers of federal regulation, whose consequences sometimes make the former Soviet Union's Ministry of Agriculture and Pencil Erasers look like a paragon of efficiency and good sense. No doubt, you've already guessed that I think that spectrum policy is long overdue for fundamental reform. I have coined a new word – "propertyzing" – for what is needed: applying real-estate-like property rights to the spectrum.

SOME BASICS

The radio spectrum covers the range from 30 Hz (cycles per second) to 300 GHz (billion cycles per second). In essence, these are the "airwaves," which are used for an ever-expanding array of over-the-air communications, including radio and television broadcasting, cell phones, mobile radio, walkie-talkies, satellite communications, radar, microwave transmission of data and even such mundane

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electronic signals as the one that tells the garage door to open. While huge amounts of information will be carried by copper wire and glass fiber, a large part of the broadband revolution will be facilitated by over-the-air technologies.

Different frequencies of the spectrum have different characteristics that make them better or worse for various uses. For example, some are better at long-distance transmission through the atmosphere, others at penetrating solid structures.

Spectrum capacity is, in respects both subtle and unsubtle, limited; one person's use at a specific time, place and frequency can interfere with another's. Interference in the transmission of information also occurs from incidental spillovers and from extraneous sources like sunspots, lightning, poorly shielded electric motors and power transmission lines. The potential for interference is readily apparent to anyone who has ever had her garage door accidentally opened by someone else's CB radio or contended with static while driving under high voltage electricity lines.

When interference threatened the nascent broadcasting industry of the 1920s, Congress chose a Soviet-style central planning solution to the problem: the Feds would prevent interference by making all spectrum allocation decisions. President Coolidge – he of "the chief business of the American people is business" – signed the legislation.

Consequently, for the past 74 years the spectrum has been the "property" of the American public, with the federal government as its steward. Explicit private ownership claims to the spectrum do not exist. In their absence, the Federal Communications Commission is charged with managing the spectrum "in the public interest."

But there was a better solution then, which is as appropriate today as it was in 1927. To see why, consider the problematic history of government spectrum management.

HOW THE FEDS DO IT NOW

First, the FCC decides the use – say, broadcasting or cell phones or walkie-talkies – to which a range of frequencies will be assigned. Next, it sets the technical rules – transmitter power, location and the like. Then, it parcels out licenses to chunks of the defined spectrum that meet somebody's idea of the greater good. Finally, its engineers enforce the rules, mostly to minimize interference.

In the 1920s, this process was (arguably) tolerable because the practical uses of the spectrum were limited, the early users were genuine risk-takers investing their own capital, and the spectrum itself wasn't all that valuable. First-come, first-served was an acceptable method of assignment.

Since then, however, the stakes have escalated substantially. There were multiple applicants for new parcels of spectrum that an expanding economy interacting with innovative technologies made increasingly valuable. So, from the late 1920s until the late 1970s, if the FCC decided that, say, an additional AM radio station should be allowed to broadcast hog belly prices in Dubuque, the agency held comparative hearings ("beauty contests") to decide which party would best serve "the public interest" and thereby receive the FCC's free renewable license.

This process, already badly strained by the rise of television, collapsed of its own weight in the early 1980s, as the FCC prepared to assign licenses for cell phones. The agency was swamped with applicants and appealed to Congress to allow other allocation meth-

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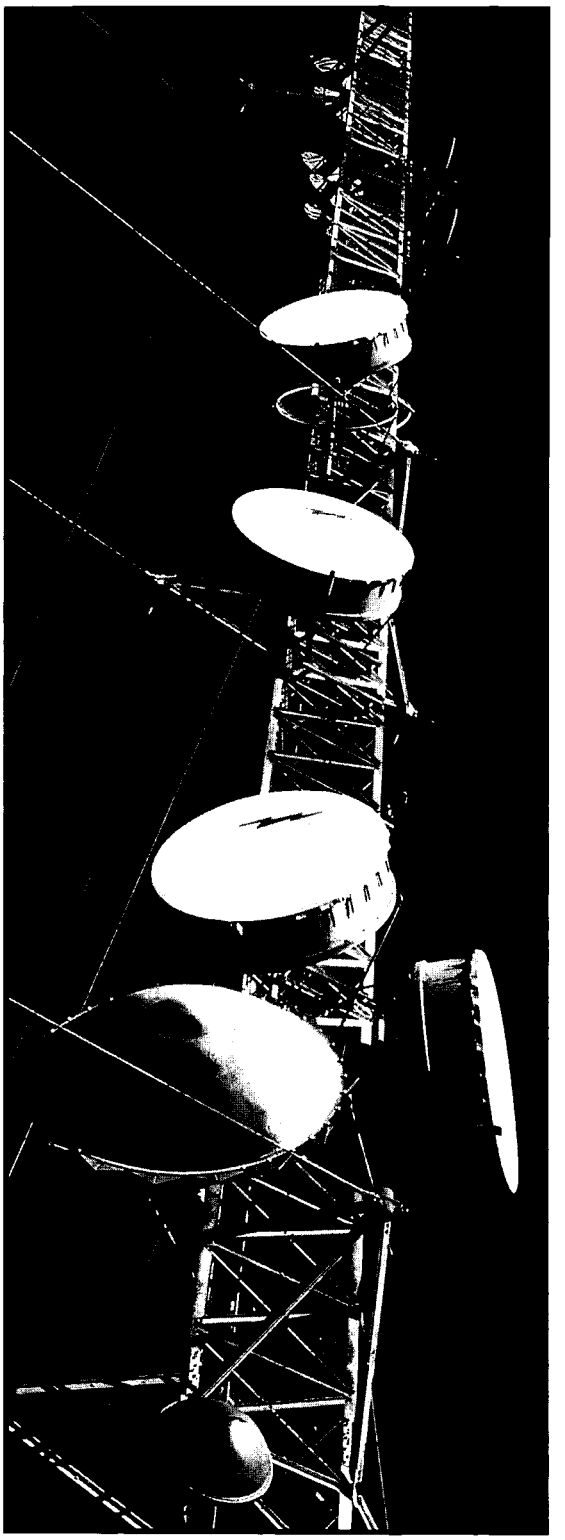
ods. Congress responded by authorizing lotteries for the free licenses, setting off a process that made the 1848 California gold rush look like a Victorian tea party.

The subsequent realization that the redistribution of property through the lottery was arbitrary (even more arbitrary than the FCC's comparative hearings) and that many winners were simply "flipping" their licenses for millions of dollars, led Congress to consider other alternatives. Auctions seemed a natural alternative, especially to economists, who had been suggesting this approach since the 1950s. But incumbent radio and TV broadcast license holders – those nice folks who so naturally deserve the free right to bombard the nation with ads for everything from Cadillacs to Cocoa Puffs – feared that auctions for new spectrum might someday be the precedent for auctioning their spectrum parcels and fiercely opposed the change.

Nevertheless, the transparent logic of selling valuable property, combined with the Congress's desperate need to raise revenue in the deficit-ridden 1990s, led the Congress to authorize auctions in 1993. As of February 2001, 32 auctions had been held, many of them for cell phone spectrum use, raising $42 billion in revenues. Despite some glitches – a few bidders couldn't come up with the cash – the auctions have been a success. Cell phone use has exploded; more than a third of total United States telephone "lines" today are cell phones. Yet despite the success of the auctions, they have affected only a small fraction of the useful spectrum.



GLORIA H. CHOMICA/MASTERFILE

THE CONSEQUENCES OF MUDDLING THROUGH

Consider the sheer hubris of Congress's vision: For the entire geographical area of the United States and for the entire range of the spectrum, the Congress expects the FCC to

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know exactly the right uses of the right bands of spectrum in the right places using the right technologies and by the right parties. Wait, there's more: As new technologies arise, the FCC will naturally recognize their worth and unerringly allocate, or even re-allocate, the right amount of spectrum to accommodate them. Of course, if Congress finds that the FCC does not have some of the pieces properly placed, our elected public servants will set things right in the blink of a lobbyist's eye.

To comprehend the challenge implicit here, imagine that private ownership of real estate were not permitted in the United States and that the entire land mass of the United States were subject to the decisions of a government commission as to the specific uses to which specific land parcels could be put, the technologies that could be used and who would be allowed to use the land rent-free, with indefinitely renewable leases.

As you awaken from that nightmare, consider the consequences of the conscious application of this "model," day after day by the Congress and regulators. All too often the FCC has discouraged competition, has favored incumbents over entrants and innovators, and has been slow to embrace new technology – all the while claiming that its decisions and actions were "in the public interest." Its decisions have sometimes taken years; court appeals have stretched them yet longer. Competing claimants have spent large sums trying to convince the FCC and the Congress of the wisdom of their positions. Indeed, a whole industry of lobbyists, forensic engineers and litigators stands ready to help.

The public has been the biggest loser. For example, in the name of encouraging local orientation for television in the early 1950s, the FCC assigned channels in a way that made it nearly impossible to form national networks beyond the three incumbents. In the 1960s and 1970s, again in the name of localism (really the protection of incumbent local television stations), the FCC impeded the expansion of cable television, which would have brought more programming. Then in the 1980s and 1990s the FCC and the Congress impeded the expansion of locally based ("wireless cable") and satellite-based ("direct broadcast satellite") alternatives to incumbent local cable companies.

The FCC delayed the initial rollout of cellular telephone service by 10 to 15 years and then licensed only two carriers per region. Further, the FCC insisted that one of the two carriers in the large metro areas (where the service was initiated in the early 1980s) be the incumbent wire-line telephone company, which reduced the competitive pressures that cell phones would bring to good old Ma Bell and her heirs. By a conservative estimate, this delay reduced national productivity by a cumulative $86 billion.

The FCC's national allocation patterns of spectrum for mobile radio uses have meant that forestry communications allocations have lain idle in New York City, while its allocation of spectrum for taxicab communications has been idle in Idaho. The agency has an unerring instinct for really knowing how to spread around the waste; a large swath of spectrum is assigned to the nation's public schools and has largely lain unused.

The FCC's management process, combined with the free licenses that have characterized most of the FCC's allocations and assignments, have (not surprisingly) yielded "shortages" of spectrum for current uses. (If Rolls-Royces were free, they, too, would be in short supply). It is now common for FCC officials to speak of a "spectrum drought." And, ironically, the FCC's mismanagement has created a second rationale for continued

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government regulation: with the airwaves in such great demand, you obviously need really, really smart federal bureaucrats to figure out where and how to use it.

For First Amendment zealots, there's another downside to the FCC's allocations: the spectrum "shortage" provides a justification (unfortunately upheld by the Supreme Court) for the FCC and the Congress to impose content obligations on radio and television broadcasters that would be considered outrageous violations of the Bill of Rights if applied to print media.

Ironically, clumsiness or incompetence has not been a significant source of these policy errors and implementation gaffes. The FCC has been staffed by knowledgeable, hard-working individuals, and much of the leadership has been highly capable. But the tasks assigned by Congress, helped by its good friends in the telecommunications biz, are impossible to perform well. Gathering all of the necessary information, processing it and making the right decisions expeditiously – and then doing it again and again, as technology and economic conditions change – is simply not something that government is built to do.

The FCC delayed the initial rollout of cellular telephone service by 10 to 15 years.

A BETTER WAY

Real estate provides an instructive parallel. In principle, one person could easily "interfere" with another's use of real estate by trampling the grass or simply wandering around uninvited. Our system of property rights is so ingrained, however, that we naturally think of such "interference" as trespassing or burglary. As a consequence, such transgressions don't occur often. Occasionally, we may have to sue a neighbor to trim a spreading oak tree or call the police to deal with an intruder. But such exceptions only prove the efficacy of the rules.

Or think of pollution. Again, these are "interference" issues, usually exacerbated by multiple emitters, like cars, and multiple receptor households. Accordingly, enforcement of property rights to have clean air around one's home is more difficult. But reasonably effective legal and administrative mechanisms do exist to "internalize" the costs of interfering with other people's property.

More generally, with well-established property rights in real estate, owners can easily buy, sell, lease or rent and adapt to changing economic and technological conditions. It is a market-based system that few – Proudhon is long gone, after all – would want to change.

PROPERTY RIGHTS IN SPECTRUM – A FRESH START

Imagine the following "clean slate" regime:

The property right (in perpetuity) would be expressed as the right to transmit over a specified spectrum band, so long as the signals do not exceed a specified strength beyond specified geographic boundaries during a specified time period. As part of that property right, owners would have the right to be free from interference from "adjacent" spectrum. Owners, including government agencies, would be free to subdivide, buy, sell or rent parcels to create aggregations over geographic areas, spectrum bands or time periods, so long as their actions were consistent

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with the other laws that affect business transactions, like the antitrust laws.

Owners would also have the right not to use their parcels, as is true for owners of real estate. Nonuse might make sense if, for example, spectrum use requires investment in complementary facilities and the owner expects that technological change or uncertainty about technological standards could render current investments obsolete.

An interim "expert" agency would be necessary for configuring the initial set of property parcels, which would then be auctioned. Even if the expert agency's initial configurations weren't ideal, the winning bidders could subsequently buy and sell in order to reconfigure their parcels. As new technologies opened new possibilities and as economic demands for spectrum changed, owners would be free to reconfigure – presumably with the help of brokers who would make markets in spectrum.

A claim that another transmitter was interfering with transmission rights of a parcel holder could be addressed through negotiations or through the courts. In light of the technical aspects of the issues, there might even be a role for specialized government arbitration. If the numbers of interferers or encroached-upon parcel holders were large enough that private enforcement through negotiation or the courts was too burdensome, alternative mechanisms – government enforcement of the private transmission rights, administrative methods for dealing with "polluting" transmissions from multiple incidental sources (like high voltage lines or car motors), perhaps even "zoning" of bands or areas – might evolve.

Government agencies could bid for and become owners of spectrum, just as they currently own real estate. Current public uses of spectrum – public radio and TV broadcasting, defense and public safety communications, emergency communications channels, open forum ("citizen's band") channels, radio astronomy – could continue, so long as taxpayers found these uses sufficiently valuable that they were willing to pay, just as they now pay for schools, parks, emergency safety services and the like.

HOW TO GET FROM HERE TO THERE

Imposing this clean-slate structure from scratch would be politically impossible. There are tens of thousands of incumbent holders of FCC-issued licenses. Despite the formal absence of private property rights in spectrum, virtually all license holders treat their licenses as property. Indeed, many bought their licenses indirectly by purchasing companies that already owned licenses. Hundreds of billions of dollars of investments in facilities, equipment, personnel and brand-name reputation are intertwined with those licenses.

But we could accept the reality of what started as an arbitrary property distribution and then build on it in the name of the greater good of economic efficiency. The FCC's licenses constitute a set of de facto properties, with protections against interference. Unfortunately, the licenses are often defined in terms of inputs (the power of a transmitter, the height of the transmitting tower) rather than in terms of a signal's strength beyond a territory perimeter. Nevertheless, these licenses could simply be assigned in perpetuity, as is, to their incumbent holders, with the existing protections against interference.

The owners of these licenses could then subdivide, sell or rent their parcels. Further, they could adjust their input combinations so long as they did not violate interference restrictions, or they could negotiate arrangements with transmission "neighbors." These

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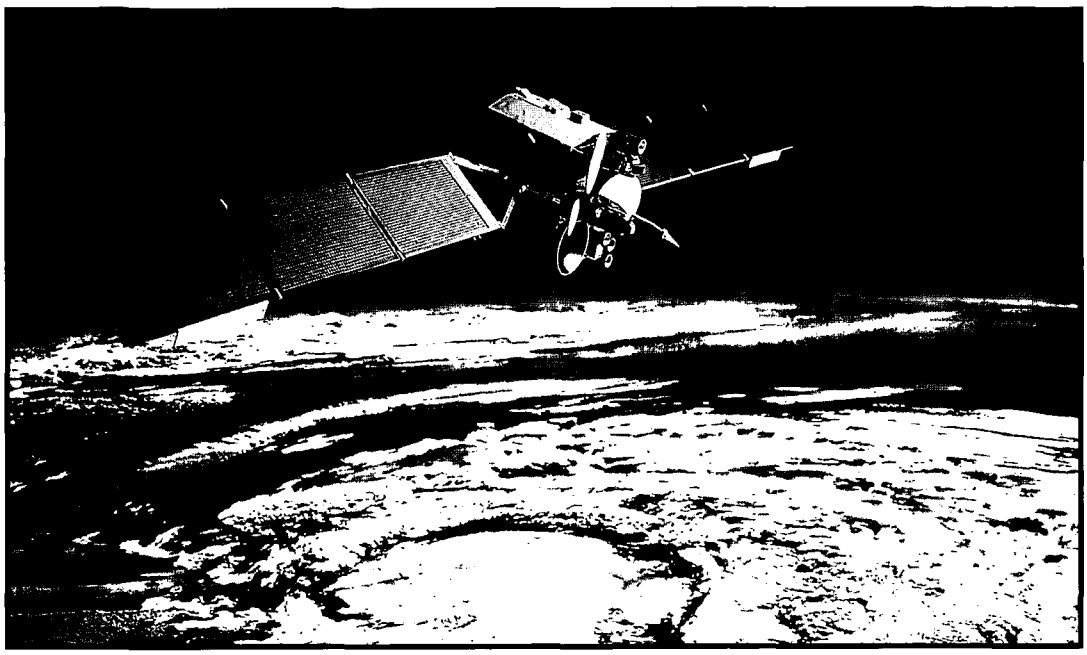

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adjustments would transform the input-based license system into a beyond-boundary signal-strength limit system of true property. The FCC could hasten this process by redefining the input-oriented licenses into roughly equivalent output-oriented licenses. After the transition period, disputes would be referred to the courts rather than to the FCC, and the FCC would transform itself into a "pollution (read: interference) control" agency, with economic efficiency as its goal.

Government agencies would receive the same property rights to their current spectrum licenses. But Congress could insist that the agencies realistically evaluate their needs and auction the surplus. The government currently holds a claim on about a third of the (currently) usable spectrum, which is substantially in excess of what's justified. The Congress partially succeeded in the late 20th century in legislating disposals of surplus military real estate. With fewer jobs at stake it might well have an easier time disposing of surplus spectrum in the early 21st. The market prices for spectrum that emerged would provide a valuable benchmark for the Congress and spur disposal decisions.

Some additional (modest) intervention – a national registry for spectrum ownership – would help buyers and sellers identify potential counterparties and help property owners identify sources of interference. (Surprisingly, despite the FCC's stewardship model, it does not maintain a roster of all licensees.)

THE BENEFITS

In a property rights regime, the owners of spectrum could flexibly adapt their uses – for broadcasting, telephone, data transmission, mobile radio and any new uses that might arise – to new technologies and new economic demands. A spectrum "drought" would be impossible; markets would clear through price rather than government fiat. The scarcity justification for the First Amendment restrictions on broadcasting would vanish.

Of course, entrepreneurs would make some mistakes. But any objective reading of the FCC's seven-decade stewardship of the spectrum suggests that markets could hardly

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do worse. For one thing, markets for spectrum would be far less likely to discourage innovation than a system where incumbency and stasis were intertwined.

With the FCC (and the Congress) removed from the processes of spectrum allocation and assignment, radio and television over-the-air broadcasting, cable transmission, local microwave (wireless cable) transmission and satellite-based transmission would be unleashed to compete. Similarly, cellular telephone and other mobile communication services would be freed from regulatory shackles; an even greater cornucopia of competitive innovations would surely follow.

THE DOWNSIDE?

Objection 1: With spectrum as private property, the "public interest" would no longer be served and public uses of the spectrum would be eliminated.

The "public interest" is a vague, ill-defined concept. Under the "public interest" banner the Congress and the FCC have established far too many protectionist, anticompetitive, anti-innovative, inflexible, output-limiting regulatory regimes and have unnecessarily infringed on the First Amendment rights of broadcasters. Governments would still have the ability to own and use spectrum in ways that taxpayers felt were worthwhile, including national defense, public safety and public broadcasting in the same way (and subject to the same constraints) that public agencies can own and use other forms of property.

Objection 2: The scheme would mean a giveaway of a vast, valuable national resource.

This barn door has been open too long to care; it is unrealistic to believe that incumbent holders of licenses could be induced to give them back. This is especially true since many spectrum licenses have already turned over in private markets for gigabucks.

Auctions of relatively vacant spectrum could still yield revenue. But the myth that the spectrum is still effectively owned and controlled by the federal government is just that: a myth. It is possible, however – though far from certain – that more efficient use of a fully propertyzed spectrum could yield some tax revenue.

Objection 3: Under a property rights system, only the wealthy would own and use the spectrum.

The current holders of FCC licenses – including large corporations like GE (NBC), Viacom (CBS), Disney (ABC), Sprint, Verizon and SBC – are not exactly the meek and the poor. The FCC stewardship and licensing system has in fact meant severe limitations on general access to spectrum use, and the limitations have favored rich individuals and sizable companies.

By contrast, a system of spectrum property rights would look more like real estate; smaller units of spectrum would be available to anyone who could pay the market price. Though spectrum ownership would surely mimic the unequal distribution found for other kinds of property, a property rights system would mean some democratization of this valuable resource.

Objection 4: Large corporations would buy large blocks of spectrum and acquire monopoly positions in telecommunications.

The antitrust laws, including prohibitions on mergers that create or enhance market power, would apply to spectrum markets, just as they apply to most other markets in the United States.

Objection 5: Since the spectrum is finite and scarce, government management and allocation is necessary.

Virtually all useful resources are scarce. The United States economy is organized

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around the general principle that private ownership and decision-making with respect to resources yields the best outcomes. Spectrum is fundamentally no different.

The past policies of the Congress and the FCC have meant that zero prices have been charged for the licenses to use the valuable spectrum resources. It is not surprising that there are "shortages" or "droughts" of spectrum at zero price. But these false shortages, created by misguided policies, aren't a justification for continuing those policies.

Objection 6: The interference problems of spectrum use can be solved only through government management of the spectrum.

This is semantics. Government would still play a secondary role, through individuals' use of the courts to enforce their property rights. Government would also play a role in dealing with more widespread "pollution control" and "zoning" issues as they might apply to spectrum – albeit a far more limited role that would be guided by efficiency and benefit-cost principles. If the government can prevent somebody from building a slaughterhouse next to the Plaza Hotel in New York, it can also enforce efficiency-based rules on private spectrum use.

Objection 7: Since spectrum uses extend across national boundaries, government management of spectrum is necessary to achieve coordination and harmonization.

Much spectrum use involves local transmissions that have minimal consequences across national boundaries. For those spectrum uses that could have international consequences, some international coordination is needed to minimize interference problems. But that coordination does not require Uncle Sam to dictate use.

Objection 8: Since the FCC is already auctioning spectrum and easing restrictions on its use, further action is unnecessary.

Though the auctions and eased restrictions of the 1990s were welcome improvements, the changes have applied to only a small fraction of the usable spectrum. The remainder is still encumbered within the FCC's "public interest" regulatory regime. And even for the slivers of spectrum that have been auctioned, use and service restrictions still apply; a full system of property rights is not in place.

ANYONE FOR PIE IN THE SKY?

Plainly, any change in a decades-old public policy that affects every American in some way and some influential Americans in very big ways would be hard to change. But converting the now-uncertain rights of current de facto spectrum owners into real property rights could change the political equation. If – and this is a big "if" – a wider constituency could be convinced that the productivity gains associated with more efficient use of spectrum were large enough to offer widespread benefits reasonably rapidly, change might be possible.

So, how do we get from here to there? For the short run, a major ingredient of the recipe is clear: auctions, auctions, auctions. In addition, the FCC should do everything that it can do endow spectrum parcels with flexibility, fungibility and transferability. If we are lucky, enough stakeholders will see the advantages of – or at least not resist – a more competitive propertyzed spectrum. For the longer run, Congressional action will be needed to bless this brave new world of property rights in spectrum.

One thing is clear, though: Unless our society finds ways to adapt and allocate spectrum flexibly and continuously to the new realities of technology, the rapid technological progress in telecommunications that we have recently taken for granted will be at risk.

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The Economics of Wolf

By Erwin A. Blackstone, Simon Hakim and Uriel Spiegel

At then-President Clinton's behest, Congress appropriated funds to hire an extra 100,000 police officers. But one might ask whether the money was well spent; the police provide many services, like response to burglar alarms, that on first glance seem public but are really private in nature. If the police could shed the nuisance of responding to false alarms, some 35,000 officers could be freed to chase alleged perpetrators.

Nearly a half century ago, Paul Samuelson elaborated on the idea of goods and services that would not be created in optimal quantities by free markets – for example, national defense. Without government to force all to share the cost, each person would have a strong motive to become a "free rider" who got to hide behind all those Abrams tanks, F-14 Tomcats and Patriot missiles free of charge.

Another Nobel Prize winner, James Buchanan, elaborated on Samuelson's idea by defining a "club good," a narrower sort of public good. For pure public goods, the size of the consuming group is the entire society. In the case of a club good, the group is smaller and the value of the good to individuals declines with the size of the population

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and the distance from the source of supply. Think of an urban park, for example.

Such services may incorporate public and private attributes. Public intervention is easily rationalized when one of the following conditions exists:

- The size of the interacting group is large, and output is indivisible. As such, exclusion is impossible or very expensive and free riding is possible.
- The good yields significant positive or negative externalities.
- The good exhibits significant economies of scale that yield a natural monopoly.

How do emergency services – fire protection, police response to burglar alarms, ambulance services, Coast Guard sea rescue – fit in? With all these services it is unclear before the fact whether they are public or private. Such a determination can be made only after the service is actually provided.

When a real break-in occurs, for example, the public interest requires a police response to catch the intruder. After all, apprehending burglars diminishes the pool of miscreants and reduces the probability that others will become victims. Detention also deters future crimes by raising the cost of criminal activity.

On the other hand, response to a false alarm is an ordinary private good, and free market economists would be quick to conclude that government intervention would lead to waste. If a potential victim makes an error and a signal is dispatched, there is no obvious reason for the public to pay for a police response. The same principle holds for alarm system malfunctions. Indeed, there is no better case for government response to false alarms than for the government to provide car towing services on private driveways.

The key distinction between responding to a car stuck in a driveway and responding to burglar alarms is that the latter has both public and private attributes. Before the fact, response is a public good at a probability level of, at most, 6 percent, since no more than one alarm in 16 turns out to be the real thing. Only after the fact does it become clear whether a public or private service was appropriate.

THE FALSE ALARM PROBLEM

We chose police response to alarms as a case study for all emergency services. Alarm systems are purchased from private dealers, who sign up alarm owners for monitoring by private central stations. Large dealers usually do their own monitoring, while smaller ones contract out the service.

When an alarm is activated, a signal goes to the central station that monitors the alarm. When the central station suspects foul play, it requests police response. More than one officer is typically required to provide backup in case an intruder is still at the scene. Once dispatched, the police will typically proceed to the site, even if the central station subsequently sends out a cancellation notice.

The data show that 94 to 99 percent of all

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activations are false. The percentage was even higher in DeKalb, GA, where the police found that only 39 out of a whopping 144,000 alarm calls logged in the year 2000 were for actual burglaries. Ironically, alarm ownership increases annually by a substantial 8 to 10 percent, yielding an almost identical rise in false activations.

THE TELEVISION BURGLAR ALARM IS HERE—KNOWN OFFICIALLY AS THE "DICK TRACY TELEGUARD".
DIET SMITH, THIS COULD BE BIGGER THAN THE 2-WAY WRIST RADIO!
Reg. U. S. Pat. Off.
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Roughly three false alarms in four are caused by subscriber error, another 10 percent by equipment malfunction and the remainder by weather or telephone problems. On average, each system activates falsely 1.3 times a year. Commercial alarms are activated at three times the residential rate. Banks, schools and municipal facilities are the worst offenders, falsely activating at seven to ten times the residential rate.

The cost of responding to false activations includes manpower and vehicle time. We calculated the average cost to the Philadelphia police department for alarm response in 1995 to have been $28 for 151,000 activations, of which 97.4 percent were false. The average cost for Dade County, FL was $24 for 121,717 false activations in 1995, while Reno, NV suffered 11,185 alarm calls at an average cost of $72. The list goes on, with Phoenix logging 47,075 activations at $73 each and Salt Lake City enduring 8,213 false activations at an average cost of $60.

Portland, OR, estimated that in 1998 the equivalent of 45 full-time officers were needed to respond to the city's false activations. Winston-Salem, NC, used the equivalent of seven officers, Philadelphia, 52, and Los Angeles, 100. Nationwide, false alarm calls for police response constituted 10 to 20 percent of all calls. In Palm Beach County, FL, (home of the hanging chad and the butterfly ballot) the percentage was an astounding 23.6 percent.

Police budgets rise at less than 3 percent annually, while false alarm response rises by almost 10 percent. Hence, the price of false alarms includes not only major outlays for police personnel but also the diversion of police officers from other tasks.

HOW THE COPS COPE

Police have reacted to the false-alarm problem by imposing high or escalating fines for repeat false activations, ceasing to respond to repeat offenders, educating alarm activators on how to improve their systems, imposing registration of alarms and requiring dispatchers to use 900-number lines that bill modest fees for each call.

The normal practice is to collect an annual registration or permit fee of $10 to $50 for alarms. The police typically allow three free responses annually to false activations. In Montgomery County, MD, the fourth false

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activation costs $50, and the price escalates for additional false activations to as high as $1,000 for residential and $4,000 for commercial establishments.

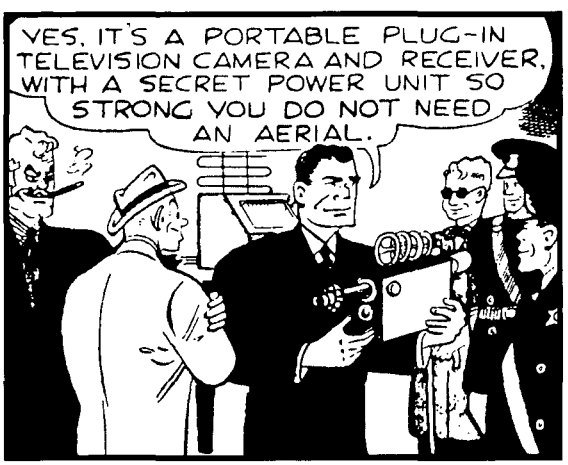
Many ordinances introduce cumbersome provisions. In Vancouver, BC, the first three responses are free, but the fourth for a residence is $75 and for commercial users $125 to $250, depending on the size of the business. The next three are free, and the next is double the amount of the fourth (Of course, false alarms in leap-year months beginning with the letter N incur a 16 percent surcharge...)

Wait – this gets better. In Palm Beach, the first two false alarms were free in 1999. The third and fourth were priced at $25, then response was suspended and a fee of $50 was charged for reinstatement of registration. The fifth and sixth alarms were priced at $25, but after the sixth $100 was charged for reinstatement. The seventh and eighth false alarms were priced at $25 with a $250 reinstatement fee after the eighth. Additional false activations required the same $25 fee, but after the 10th, the reinstatement charge was $350 and after the 12, $500.

A new simpler ordinance, passed in 2000, complicated matters in a different way. Now in Palm Beach, the registration fee for alarm users depends on the total number of false activations logged by customers of the dealer who services the alarm. Thus, the registration fee of any subscriber depends on the number of false alarms by the other customers of the same dealer.

Another practice is simply to stop response after a certain number of false activations. In Redmond, WA and Santa Ana, CA the police stop responding after the sixth false activation in a calendar year. Miami Beach suspends after the seventh.

Phoenix pioneered the use of educational programs for chronic alarm abusers. The police hold classes to explain the duties of alarm owners to keep their equipment working properly, the details of the alarm ordinance and some means to prevent false dispatches. The alarm industry also initiated two partnership programs with the police though which frequent false activators were identified and educated in order to prevent further occurrences.



Toronto charges $77 for all false activations and stops responding after the fourth within a year. The immediate effect after the ordinance was adopted in 1996 was a shift of more than 90 percent of subscribers to private guard response, resulting in a 60 percent reduction in false-alarm incidents. Clearly, the high pricing of police response was successful in creating a competitive private response market. Further, Toronto's ordinance makes the private central station responsible for the fines.

The alarm industry is challenging this get-tough practice in the courts, and the issue is still in litigation. Charging the central station reduces transaction costs for the police, who can avoid dealing with thousands of false activators. However, if a central station does not pay its fines, all of its subscribers lose

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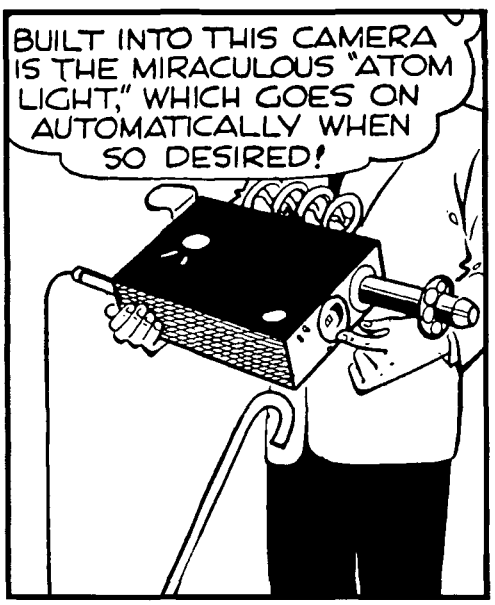
police response, including many who did not falsely activate their systems.

IS IT WORKING?

The basic problem here is that no one except the police has a direct interest in reducing false alarms. The typical alarm owner falsely activates his system 1.3 times a year. And since



most communities allow three false activations annually, the alarm owner incurs no charges. Repeat activators are often municipal facilities like schools that do not have to pay fines, or commercial establishments that pay the fines and write them off as a routine cost of doing business. One Illinois bank budgeted $12,000 annually for false-alarm fees.

Alarm dealers, for their part, view police response as a gift. They sell the hardware and then charge monthly fees for managing a response system that is largely provided by the police. Dealers consider false activation to be someone else's problem and apparently have little interest in spending on a collective solution. Hence, dealers and alarm associations contest police efforts to limit response except for nonpayment or for repeat activators or to shift responsibility for fines to dealers.

We find it ironic that private industry prefers government intervention to encouraging a new form of business – companies offering comprehensive alarm response – to develop. Central stations today are supposed to verify that an actual intrusion took place and only then contact the police. One explanation for their reluctance is the risk of a "false negative" – a call that is verified as false even though a real break-in did occur. In such cases, central stations may be legally liable. So they are inclined to dispatch the police whenever there is the slightest chance of a break-in.

The reflexive fix – to discipline careless use of alarms by ceasing to answer calls – is inappropriate from the economist's perspective. Suppose a person has a habit of kicking his refrigerator and breaking its door. Maintenance services are happy to fix it as long as the ill-tempered refrigerator offender is willing to pay. Indeed, the more calls, the better it is for the repair company. By the same token, there is no reason to deny response to a false activation as long as the violator pays the full cost.

The police often charge higher fees for responding to alarms at commercial establishments than at residences and exempt municipal facilities from charges. In all these cases, prices are divorced from cost because there is no market to drive the price structure. Below-cost response induces carelessness and drains police resources. Schools pay for electricity and textbooks, so why not for police response to false alarms?

Similarly, local ordinances impose high charges to discourage false activators. That deterrent seems intuitively correct, but it, too, causes a misallocation of resources. If the charge is higher than the real cost to the po-

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lice department, some households and businesses will refrain from buying alarm systems and some owners will not activate their systems. Society will then suffer from a lower level of security. By the same token, charging less than the real cost artificially encourages the use or abuse of alarm systems.

Most communities use escalating fees for response to repeat false activations. If the marginal cost to the police remains the same, then raising fees yet more will simply discourage the purchase and use of alarms whose benefits exceed their costs. The evidence suggests that repeat visits to the same address do not cost more to the police – and may well cost less.

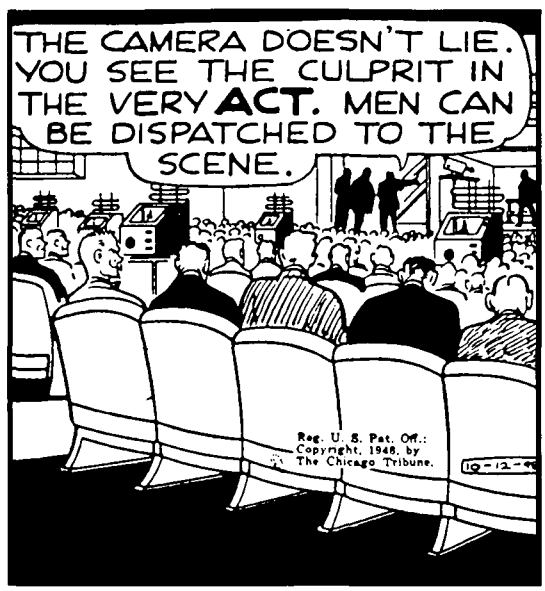
When the police respond to false activations, people who do not own alarms and alarm owners who are careful about their systems subsidize the careless. There is no justification for such cross-subsidization. Indeed, since the cost of false alarms is imposed on the police (and thereby on the community), there is no justification for any free responses. False activations should be charged from the first incident.

WHAT WOULD ADAM SMITH DO?

The solutions implemented by police departments and the alarm industry have, at best, put a Band-Aid on the false alarm problem. In our view, the problem can be overcome only if the hybrid nature of the service is recognized and an appropriate competitive market solution for the private segment of the service is implemented.

Efficiency requires that both the public and private sectors be involved. Private response should be dispatched to all activations. In the case of an actual intrusion, private security at the scene can request police response. Since the police would no longer respond to false activations, they would be more motivated to respond rapidly and efficiently to actual events – which are, indeed, a public good.

In an efficient market, each alarm owner would contract with a private company for such a service. Since response to alarms is labor intensive, the potential for economies of scale are limited. So, in large urban areas, one would expect that many companies could


THE CAMERA DOESN'T LIE. YOU SEE THE CULPRIT IN THE VERY ACT. MEN CAN BE DISPATCHED TO THE SCENE.
Reg. U. S. Pat. Off.: Copyright, 1948, by The Chicago Tribune.

provide the service efficiently – a precondition for a competitive market.

Competition among providers would presumably spur innovation and reduce costs. What's more, providers would be able to use lower cost labor – security guards as opposed to the police – as initial responders. A competitive market would replace a public monopoly, and cross-subsidization between alarm activators and others would cease. Consumers would presumably also get the benefit of market-driven variety, paying more for faster, more reliable responses.

Some interesting implementation questions remain. Should the police stop responding to burglar alarms under all conditions?

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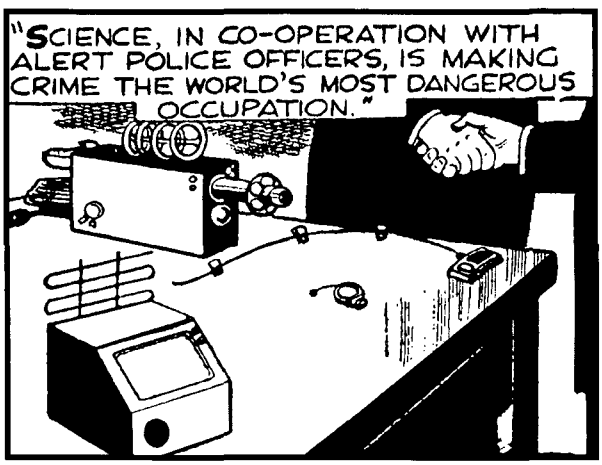
CRYING WOLF

What should happen if no private response emerges in a sparsely populated area?

The delivery of service by the public police monopoly might not be efficient. Unfortunately, in small markets consumers would have to endure the lack of competition. But there may be a more positive role for public enterprise here than one might first expect.



Recall that regulated monopolies are undesirable because they may produce inefficiently, may cross-subsidize and may erect entry barriers to maintain their monopoly power. Hence, if the police wish to retain the service as a non-monopoly, they need to price it at their long-run marginal cost and allow others to provide the service under competitive conditions. The police probably enjoy "economies of scope" in the sense that providing alarm response could lower the cost of other services and the other services could lower the cost of alarm response. As a result, we think consumers would gain if the police were allowed to compete.

Privatization of alarm response could take two forms. The police could contract out the service to a private company to serve the entire or part of the jurisdiction, much as municipalities have granted franchises to cable television operators. Alternatively, entry to the response business could be open to all interested parties. The latter is surely preferable, since it would short-circuit all the standard problems of creating appropriate incentives for government-regulated monopolists to deliver services at prices that reflect cost.

ADAM SMITH LIVES

Las Vegas utilizes a system close to our model. In 1991 the chief of police adopted a non-response policy on his own initiative. Before the change, responses took 45 minutes on average and involved two officers. Only 1 to 2 percent of calls were valid alarms. Since then, the police have responded to alarms only when dispatched by an agent at the scene. Police response is now faster.

The agents are usually guards from a private response company. They remain outside in case a crime is in progress, watching the exits until the police arrive. The annual budgetary savings exceed $600,000, with no apparent sacrifice in security. In fact, the burglary rate diminished from 1,600 per 100,000 residents in 1990 to 1,187 in 1998.

In 1999 Salt Lake City police responded to some 8,300 alarms, 99 percent of which were false. Near the end of 2000, the city adopted the Las Vegas model and, within months, seven companies were offering private response for fees that were substantially less than the $60 average cost for the police. The private response time ranged from 2 to 20 minutes, compared with the 40-minute average the previous year. Most striking, perhaps, the number of false alarms fell from 773 in December 1999 to just 3 in December 2000, as alarm owners adapted to a world in which they paid for response service.

The bottom line: Free markets work in the oddest places, given the chance. M

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A Nobel Round Table

You gotta be there to get the full flavor of one of Michael Milken's Global Conference tête-à-têtes with Nobel Prize winners in economics. But here's a heavily edited (for space and syntax) sampling from this year's conference, held March 20-21 in Los Angeles.

— Peter Passell

MILKEN INSTITUTE (ALL)

DONALD STRASZHEIM (President of the Milken Institute): Let me start by introducing the Nobelists.

On your left is **Gary Becker** from the University of Chicago. Gary got his prize in 1992, and just last year was awarded the National Medal of Science. Next is **James Heckman**, also from the University of Chicago, who received his Nobel Prize last year. Next is **Lawrence Klein** (Nobel class of 1980) who is a professor from the University of Pennsylvania and, incidentally, my old boss at Wharton Econometrics. And last, **Douglass North**, professor at Washington University at St. Louis, who received his Nobel in 1993.

Now, everybody knows the moderator, **Mike Milken**. But no one here knows everything, really, that he has done. He is ranked by *Worth* magazine as the sixth leading philanthropist in the country. He founded CaP CURE, the prostate cancer research and fund-raising organization that has raised some-

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thing like $75 million for prostate cancer research in the last seven years, and is now the largest private funder of prostate cancer research in the world.

Mike also chairs the Milken Institute. As if that weren't enough, Mike is the co-founder of Knowledge Universe, a company whose mission is to incubate and invest in companies that enable the New Economy. And he is also the author of a unique series of cookbooks, *The Taste for Living*, designed to provide guidance for a healthier diet.

MICHAEL MILKEN: Thank you, Don. Well, it is March of 2001 and what a difference a year makes. A year ago, for one brief moment, Cisco Systems had the highest value of any corporation in the world. But when you called your broker and told him to buy the stock, did you ask him to buy Cisco, the telecommunications network company, or Sysco, the restaurant supply company?

Had your broker understood it as the restaurant supply company, your stock would now be up 40 percent. Had he misunderstood you, and thought you meant the network equipment maker, you would have lost 60 percent.

One of the points I want to make today, one I first raised 30 years ago, is that we have a market of stocks – not a stock market. All stocks are not equal, and the Cisco/Sysco confusion brings that home.

Are we moving in the direction of 1974? You might remember that famous headline in one of the leading business news magazines of that December: "No one will ever buy a stock again." The stock market fell almost 50 percent in two years – only to go up 80 percent in the following two years. Or are we going to spend a long time trying to get back to where we once were?

Gary, would you like to start us off?

GARY BECKER: Let me preface my remarks by saying economists are very poor short-term forecasters. But I think one has to draw a distinction between stock values and the real economy. And the stock market – the Nasdaq, not so much the Dow – has had an enormous fall. The Nasdaq is down, what – 60 percent or so from its peak?

But the real economy, the major determinant of the well-being of most people, is measured by employment and productivity. And while the growth of the economy has slowed, unemployment remains quite low.

My own forecast – and remember my first remark about economists' forecasts – is that this will be a relatively sharp but short recession. The fact that the stock market has tanked does not mean that the economy will end up in a similarly disastrous situation.

MILKEN: You are suggesting that the real economy continues forward and we have had a re-evaluation of the future growth of the technology sector. Jim, what's your view?

JAMES HECKMAN: I agree with Gary about the fundamentals. Looking at productivity growth in the last four or five years, we have seen a very important sustained increase – one that goes above the trend between 1970 and the early 1990s. I do not see any substantial impairment in the fundamentals at this point.

MILKEN: Four years ago, the chairman of the Federal Reserve said that there was an "irrational exuberance" in the marketplace. At that time, the Dow Jones Industrials were selling at 6,400 and the Nasdaq was at 1,300.

We have had a great deal of volatility since. Yet both of these marketplaces are still up 50 percent. Doug, are we still in a period of irrational exuberance?

DOUGLASS NORTH: Oh, I think we are going to come down some more. The question that interests me as an economic historian, is

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whether this is like past cyclical phenomena.

MILKEN: It took 25 years for the stock market to get back to where it was in 1929 [after the Great Depression struck]. Where do you see us on a historical basis?

NORTH: Certainly, the information revolution of the past 25 years has some parallels with other great expansions – like the boom following the invention of the automobile or the dynamo in the 1920s. But I am not sure that we have a parallel from the past that tells us what is going to happen this time. I am sure we are still in the midst of the revolution in information technology. I think that makes a difference with respect to what is going to happen. We may have a very sharp recession. But underlying the cycle, there are still possibilities for expansion related to as-yet-unexploited technologies.

BECKER: Mike, you mentioned 1929 and the long time it took to recover. But the really important events of that period were not in the stock market. The economy tanked for a decade; the 1939 unemployment rate was still over 20 percent. In large part, the stock market was not driving the economy. The economy was in terrible shape for a full decade, and the stock market reflected what was happening to it.

MILKEN: So the point here is that the economy has not changed that much. And that ultimately, the market adjusts to where the economy is – not the other way around.

LAWRENCE KLEIN: I think one should look at what has happened in comparison to 1987. Just a week ago, I was on the trading floor for a mock, after-hours trading session at the New York Stock Exchange. I asked a trader if he thought that last week's break was anything like October 1987. And he said, "No comparison. This one was much easier to handle."

Much easier because of the technology in clearing trades and handling very large transactions. And that is really the key.

I think we are all agreed that the growth in productivity is something of medium- or long-term significance. The real economy is not in such bad shape, though it is not in its best condition. The financial economy was irrational. There were very foolish valuations for a lot of startup companies without any profits in sight.

MILKEN: Let's take a quick look at the world's second-largest economy, which has been acting very differently than the U.S. economy. Unemployment has been drifting up through the past decade in Japan. It is still relatively low by our standards – in the 4 to 5 percent range. But for them, this is a dramatic increase.

Whereas government debt has dropped considerably as a percentage of GDP in both the United States and the European Union, Japan has had a significant increase.

And if we take at look at their interest rates, we notice they just lowered the rate to zero. So one could borrow the yen-equivalent of billions or trillions of dollars at zero cost. Many of us think we could find opportunities to put that money to work at a positive spread.

KLEIN: I would not say that. If you look at that slide of interest rates, you see a classical example of a "liquidity trap," which Keynes talked about 60 or 70 years ago. What Japan really needs is a lot of Keynesian medicine.

MILKEN: So if you were going to go to the Ministry of Finance today, what would you recommend?

KLEIN: Japan did quite well around 1995-1996, when the head of the Economic Planning Agency went very heavily into public works and the traditional kind of infrastructure spending. That was successful for a couple of years.

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But now I would say it is human capital that Japan needs. And if they would revamp their university system as a massive public works effort, they would do very well. Japanese K-12 education is fine. It is not so good at the university level.

MILKEN: Are their best and brightest going someplace else in the world for education?

KLEIN: We handle them at the Wharton School every day.

MILKEN: Are they returning to Japan?

KLEIN: Well, no.

MILKEN: Do you think those students from the Wharton School could solve Japan's problem?

KLEIN: Wharton is not that big.

MILKEN: Doug, what's your reaction?

NORTH: Lorrie [Larry Klein] is suggesting a long-run solution. But I think in the short run, you have got to restructure the banking system, the whole capital market in Japan, to make it viable. And they are a long way from doing that. The political system has been very reluctant to make fundamental adjustments.

An enormous percentage of banks are, in fact, bankrupt in Japan today. And until it faces up to that, I don't think Japan is going to come back.

MILKEN: Bank lending in Japan has actually decreased. So in spite of interest rates between zero and two percent, more loans have been paid off than taken out.

BECKER: The real interest rate is a bit higher than that, because Japan is one of the few countries that has experienced significant deflation in recent years. But I agree with Doug that their banking system is in terrible shape. They are not lending because equity in the banking system is very low.

I do not believe that Keynesian medicine would work. I think they've tried it, and it did not work. Their debt increase was partly the result of running large deficits in order to jump-start the economy. Japan now has a government debt-to-GDP ratio of about 1.4 or so – one of the highest in the developed economies.

Their higher education system needs reform, although as Doug says, that is more a long-term problem. Japan had enormous growth from 1960 to 1990. We should not forget that. There are great strengths in Japanese human capital: hard-working people, good K-12 education. Maybe not good higher education, but they do send one of the largest percentages of high school graduates into higher education of any country in the world.

I think human capital is a good forecaster of potential, and I am still bullish in the long run about Japan.

MILKEN: We can see what has happened to their stock market. And what you are suggesting here, really, is that their stock market has followed their economy over this period.

BECKER: Yes. I think they need to do several things – among them restructuring their

Jim Heckman (in glasses) explains it all to Gary Becker

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financial system and allowing easier access to foreign banks. There is capital out there that might be attracted to Japan if it opened up its economy. Japan is still a closed economy in many sectors, particularly in services and some manufacturing.

I agree with Lorrie: improving their higher education system would help. But it is not going to do much in the short run.

MILKEN: Look at the issues facing Japan: one of the oldest and most rapidly aging populations in the world. High but badly deployed savings. Hundreds of trillions of yen invested at negative rates of return. Equities at their lowest levels in 20 years. Interest rates near zero. Nine governments in 10 years.

BECKER: Let me just say one last thing. I think Japan has had a good tradition of taking the best and the brightest, and steering them into the best schools. So I do not believe it is true that Japan is not a meritocracy.

HECKMAN: I would not agree with Gary that Japan is a pure meritocracy. Rather, it is a corrupt meritocracy with diminished incentives.

I think there is a tremendous amount of competition at the secondary level to get into prestigious schools. But once you get in, the incentives to perform are weak. You are pretty much set for life.

BECKER: But Jim, Japanese leaders come from as modest a set of backgrounds as their American counterparts.

HECKMAN: That is right. But once you get into a leading school, society becomes quite rigid.

KLEIN: One big obstacle is the lifetime employment system. That is exactly the opposite of our labor market, where people who got downsized in the 1980s found jobs in the new technology and service sectors.

HECKMAN: Lifetime employment is a stereotype. There is an amazing amount of labor flexibility in Japan, especially in the last decade.

BECKER: But they classify workers into "permanent" and "less permanent." The less permanent workers have a lot of turnover.

HECKMAN: And it is a substantial part of the economy.

NORTH: I was in Tokyo in December, and I had dinner with some CEOs who implied that the real unemployment rate would be substantially higher if they had the flexible employment system that we have in the United States.

MILKEN: It sounds to me like there is a consensus here that one of the major assets in the United States is our higher education system. And quite possibly, it has more than offset the deficiencies in our K-12 system.

The other area we've often talked about is the difference in savings rates. While their savings rates have backed off, they still are very high compared to the United States.

When you spoke about a liquidity trap,

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Lorrie, how does that relate to the savings rate?

And Gary, you said foreign capital would be willing to invest in Japan. Well, there is $7 trillion in postal authority accounts, invested between zero and one percent. It does not seem like there is a lack of capital. It looks like there is a perception of lack of opportunity.

KLEIN: People have lost confidence in the government and they are putting their money in the postal savings system. And that is why that savings rate stops at a bottom that looks high to us, but is low for Japan.

MILKEN: In 1974, Americans lost confidence in America. We thought New York City was going to go bankrupt. The same for New York State, Con Ed and thousands of major corporations. And it took people from Canada to come down here and invest in our real estate.

In '89 and '90, we lost confidence in what is today the core of the most valuable financial institution in the world as measured by the marketplace – Citicorp. And it took a young sheik from Saudi Arabia to come in here and buy equity in it. Are you suggesting that it is going to take risk capital from outside of Japan to turn Japan around?

HECKMAN: I would not look for a white knight to ride into Japan. He would meet much regulatory resistance.

NORTH: I agree with Jim. When talking about potential reforms in Japan, foreign entry is one of the areas that I would put on high priority. It applies to the financial markets. It applies partially to the labor markets – although, as Jim said, they are more flexible than they appear. It applies, in general, to entry of foreign companies into retailing and other sectors.

Japan is not the same Japan as it was 10 or 15 years ago. But movement has been glacial. And I think that partly explains why they have been stagnating for a decade.

MILKEN: What is going to happen in the next 25 years with the one percent drop, after immigration, of people between 35 and 54 years old in the U.S.? Lorrie, do you think we are all going to be working until we are 90?

KLEIN: Or we could rely more on immigrants. Incidentally, that is one thing Japan refuses to do on a large scale.

MILKEN: Gary, I know you have done a lot of work on demographics. Why don't you tell us what is going on with the world's population today?

BECKER: The most striking development in the last decade has been this divide between the population haves and have-nots. Almost half the world's population is now in countries with birth rates that are below replacement – less than two children per woman. If this continues, these populations will begin to fall. Their growth rates have already slowed enormously.

We're talking here about every country of western Europe, much of eastern and central Europe including Russia, much of Asia, but particularly China and Japan, parts of Canada, Cuba and some other parts of the Western Hemisphere. The U.S. is just slightly below replacement. All told, that is a little less than half the world's population.

The countries with low birth rates are the rich countries. Those with rapid rates of growth are the relatively poor countries – all of Africa, India, and much of Latin America.

The countries with low fertility have aging populations, which makes it more difficult to finance traditional pay-as-you-go Social Security. That is one of the reasons why I favor individual account systems. It adds pressure to reduce the employment tax on older people. We have been moving in that direction in the United States, allowing people to continue to work at older ages without

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losing benefits. Europe has been very slow in moving in that direction, and people retire much younger.

It is a paradox. We are getting healthier, mentally and physically. Yet we are encouraging people to retire earlier.

Then there are migration issues. The arbitrage solution, if I may use financial terminology, would be to move people from poorer countries to richer countries. Some of that is going on, but there is enormous opposition to taking in immigrants in most rich countries.

You see that in the United States in our discussions with President Fox of Mexico. You see that in Europe, which resists immigration from northern Africa. You see it in European political parties whose main program is stopping immigration.

MILKEN: With populations dropping throughout the developed world, is this going to continue?

BECKER: The opposition is mainly from unions and young workers who fear their wages will be affected.

Look at the United States. We have the H1B program that allows several hundred thousand high-tech people to enter each year under temporary visas. We should be expanding that program enormously. Here we get these high-tech, well-trained people from abroad, trained at the expense of other governments. Yet it is very hard to expand these programs.

MILKEN: But demographics are going to have a significant effect on the future. Think of Russia shrinking to 100 million people. Or Europe shrinking by 10 percent in the next 50 years. Do you think that is going to happen, Jim?

HECKMAN: Those projections are right. But I think there are a number of margins you can still work to offset the impact.

There is a lot of scope for migration, even within Europe. Look at migration from eastern Europe to western Europe. Look at Italy and the issue of internal migration. The entrepreneurs in the northeastern part of Italy – a very dynamic, vigorous region – are very short of workers, skilled and unskilled. Yet there are a huge number of people in Sicily in make-work government jobs. With some policy reforms, you could ease the labor pressures in northern Italy.

So I think that the barriers are not just between the developed and less-developed world. There is plenty of scope for adaptation and adjustment within the developed world, for promoting mobility.

NORTH: We are assuming that the projections are correct. I have grave doubts about the ability of demographers to predict very far out.

BECKER: There is no doubt they have made mistakes. But the mistakes have generally been in overstating fertility, not in understating it.

I was examining the U.N. forecast that just came out. Three years ago, the U.N. was projecting that the low levels of fertility were temporary. In the latest revisions, the U.N. says, "well, it's probably permanent."

In 1988, there were about 30 countries that had birth rates below replacement. Not a single one of those countries has moved above replacement since then. And they have been joined by another 30 countries.

Or take the poorer countries of the world. The U.N. recognized that their birth rates were coming down, but they assumed they would come down much more slowly. They are going to be wrong on this new forecast. But I think they are understating the rate at which birth rates are declining.

KLEIN: The Baby Boom generation was not foreseen and there was an enormous population increase in the United States, Europe and other countries. We do not always get errors

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on one side.

MILKEN: Jim, I want to come back to what you were saying. I believe Bulgaria has lost 20 percent of its educated people under 30 years old to western Europe. Who is moving to Bulgaria?

HECKMAN: If the environment were a little better for investment, a lot of Italian and German companies would move capital to Bulgaria.

Such countries have to come to terms with their environments for investment. Italians would like very much to invest more in Bulgaria, but they fear the regulatory environment. Bulgarian policymakers are going to have to adjust in one dimension or the other – and probably all dimensions – to really be competitive.

MILKEN: What I am hearing from the four of you is we have a lack of supply of human beings in the developed world and an excess of supply in the developing world. So if the developing world could get its act together, the developed world would invest in these areas and labor imbalances would not be an issue.

NORTH: You are sliding over the question of the degree to which institutional structures can adjust to solve problems.

In Germany and France, we still have unemployment rates near 10 percent. That reflects institutional rigidity. In the case of Germany, labor-management "cooperation" has produced the highest labor costs of any country in the world. I think we have to face the fact that there is no guarantee that institutional structures are going to adjust.

BECKER: If you want to equalize incomes, returns on capital or returns on labor, you can either do it by moving labor or by moving capital; you do not need to do both.

The problem is, there are important obstacles to movements of both types. Mexico went through significant reforms since the early '80s in opening up its economy: Nafta, deregulation in some sectors, privatization in some sectors. The response has been pretty dramatic.

True, Mexican workers still see better opportunities in the United States. But there is a lot of investment going into Mexico. And, in principle, these opportunities could be created in Bulgaria and in other parts of the world.

HECKMAN: If you look at what happened in England, there has been a major transformation in the institution of unionism. The workforce is still substantially unionized, but the form of unionism changed in response to a crisis in the late '70s.

Cycles of reform follow this pattern: you enter some kind of crisis before reforms are put in place.

KLEIN: Spain was the weak link among the continental countries, with 20 percent unemployment. Now Spain is in the neighborhood of 15 percent and probably coming down. So once a country starts moving, you can break through some of those institutional barriers.

The other part of the story for the U.K. is that it didn't join the common monetary system, and therefore didn't follow the restrictive fiscal and monetary rules for joining.

MILKEN: Would you call that supply-side economics?

KLEIN: Well, not in the sense that "supply-side economics" is commonly used – the crude sense. The correct sense is to look at productivity and the real economy – not just fool around with taxes.

BECKER: Go back to the issue of high unemployment in continental Europe. Why is Europe resisting the reforms that made such a difference in Britain?

In Europe, there are insiders and outsiders.

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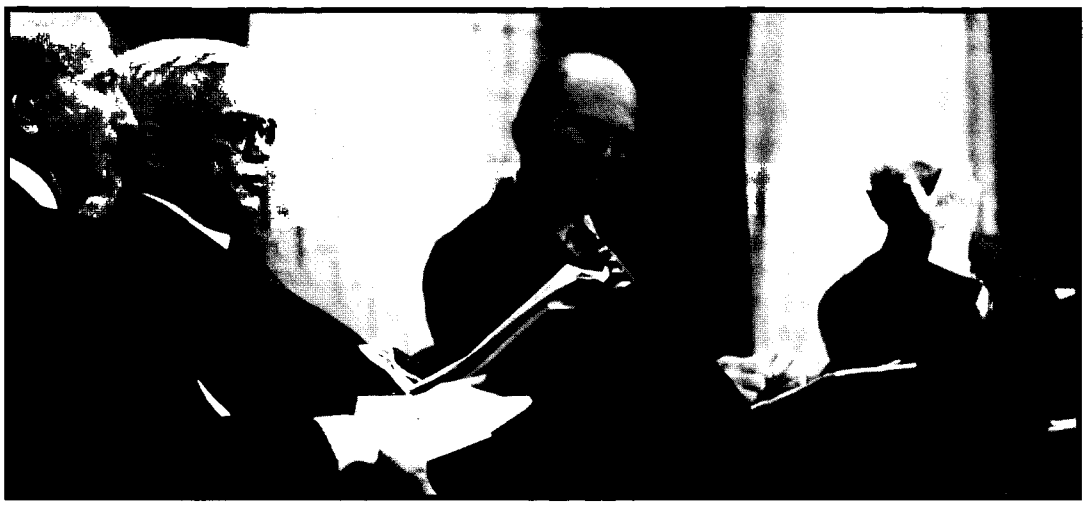

Left to right: Gary Becker, Jim Heckman and Michael Milken agree; Lawrence Klein apparently doesn't.

By insiders, I mean those people who have good jobs. They do not want to free up their markets. They have good wages. They are already in a very good situation.

Who is being hurt? As usual, the people at the bottom. In most countries, they are low-skilled people, young people, women who try to move back into the labor force after moving out, and immigrants.

The political contest is between these relatively weak individuals and the people who are comfortable with their positions, who have good jobs in Europe, and who do not want to see radical change. Germany has been trying to overcome that and has basically failed to make a dent in the system.

NORTH: Let me go back to Japan again. Here is a country that has been stagnating for 10 years. And the problem is fundamentally a political problem – the point that Gary was making with respect to Germany. I am optimistic that the Japanese are going to solve it, but my optimism is not based on any neat body of political theory. Political scientists are even more primitive than economists with respect to being able to model what is going to happen.

MILKEN: European institutions like HSBC Holdings, Barclay's and Royal Bank of Scotland have come into the United States and bought our insurance companies and financial institutions. Deutsche Bank has made a whole slew of acquisitions, as has Commerzbank. Spain's leading financial institutions are here in the United States. Dutch banks – ABN Ambro, ING Group and others – have come in and acquired many of the brand names. And I think we are all familiar with Union Bank of Switzerland and Credit Suisse-First Boston's acquisitions of the major banking and Wall Street firms in the United States.

Do you see an opportunity that the knowledge and human capital that is now controlled by European financial institutions will change Europe in the near future?

HECKMAN: Well, the question is whether or not this amounts to an escape from Europe or whether or it is going to generate sort of an infusion back into Europe.

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BECKER: We were ahead of the Europeans and the rest of the world in financial innovations. Low-grade bonds being one.

MILKEN: Securitized bonds.

BECKER: And securitized bonds. You know, options and all those things.

BECKER: So, we were ahead of them. I think there is no doubt that they are catching up with us in these techniques. You can see that not only from the companies they buy; in the last 15 years, the number of Europeans studying in U.S. institutions in business, economics and other subjects has grown tremendously.

So I do not think in the next 10 years there is going to be a major difference in knowledge between the Europeans and the Americans. The issue will arise whether the regulatory environment allows them to display that knowledge in as flexible and as productive a fashion as we do. I do not count London as Europe, because London is the United States, from my point of view, in terms of the way its economy functions.

MILKEN: Gary, some people in London think the United States is London.

BECKER: It is both. It is the so-called "Anglo-Saxons versus the Continent." And I think that is the basic difference.

MILKEN: I think it is time for some concluding comments. We have identified a number of destabilizing forces – demographics, income disparities, regulation. Are we going to move to solve these problems in the coming year?

NORTH: I am not as optimistic as many of my colleagues are.

MILKEN: So would you then say you are not optimistic?

NORTH: I am not *as* optimistic. That is a weasel word, Mike. We are entering a world we have never been in before, one that is novel with respect to so many dimensions. I am less optimistic, particularly in the political realm. And until you get a political system in place that guards economic and property rights, I think you will continue to have problems.

MILKEN: Lorrie, can you be a little bit more definite than Doug?

KLEIN: Well, I am generally optimistic. But I think we are going through a short-run adjustment now. I am not saying it will be over with next year, but it is short-run.

You cannot resist globalization; you cannot resist technical progress. But you have to learn to adjust to it.

MILKEN: Jim, what about you?

HECKMAN: I think everything we know from reforms around the world suggests that some of the problems plaguing Japan and Europe could be resolved by more flexible institutions. And I think they are being forced to become more flexible.

MILKEN: So we are going to put you in the more optimistic side of the ledger.

HECKMAN: Long run. Not a forecast for next year, but for next decade.

MILKEN: And Gary?

BECKER: Well, I am an optimist from a long-run perspective. I am not ignoring the issues that Doug is raising. But if we look at the last 50 years, we see two mega-developments. One, the great movement toward democracy, and two, the movement toward freer economies.

Of course, progress could be reversed. But I think there are powerful forces that have driven these trends. There are objective reasons why one should be pretty optimistic, although year to year, you can have a lot of difficulties.

MILKEN: Okay, we got a little hedge there at the end. But we have at least two very optimistic long-term views, one viably optimistic long-term view, and one a little less optimistic long-term view.

Thank you all for joining us this year.

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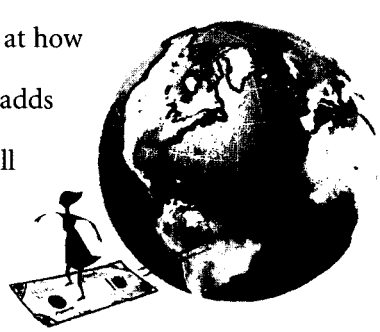
Money Makes the World Go Round

ILLUSTRATIONS BY
KEN ORVIDAS

For those who remember the Vietnam War as a defining political event, Barbara Garson's name probably comes to mind as the author of the deliciously nasty satire *MacBird*, a takeoff on *Macbeth* that gave Lyndon B. Johnson the very hard time he so richly deserved. Turns out there was a life after Vietnam for Garson, who has written a number of books examining, among other things, the sociology and economics of work from the perspective of the left. ¶ Her latest book is a smartly nuanced look at the consequences of globalism. Like Woodward and Bernstein (another blast from the past) she follows the money, in this case, her own money from a modest book advance that she invested relatively conservatively. ¶ This excerpt probably won't change your mind about the virtues and vices of global economic integration. But Garson's up-close-and-personal look at how her money is being invested in an oil refinery in Singapore adds flesh and bone to the bloodless tales that economists like to tell themselves about the triumphs of contemporary capitalism.



BY BARBARA GARSON

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Singapore and Malaysia were both colonized by Britain in the 19th century, both occupied by Japan during World War II, and both granted independence after the war. As a matter of fact, they were briefly a single independent nation. Geographically, Singapore is just another of the many steamy islands that straddle the equator between the Indian Ocean and the Pacific. It's composed of the same mix of Malays, Chinese and Indians as Malaysia and the Indonesian islands are, except that in Singapore the Chinese predominate.

I was in Singapore to look at a catalytic cracker, an oil-processing unit that Caltex was adding to its Singapore refinery with the help of a Chase Manhattan Bank loan that, in theory, was in part financed by my deposit. But I couldn't help asking, as I went about my business, how this particular tropical island had become a wealthy city-state.

My tentative explanation for Singapore's prosperity was "no corruption." When I asked Singaporeans or foreigners who lived there, their answer was unhesitatingly "Lee Kuan Yew."

Lee Kuan Yew, Singapore's first prime minister, had led the colony to independence in 1959. The former socialist immediately jailed a few of his trade-union allies and instituted a system of regulated capitalism that borrowed economically from Sweden and morally from Confucius, but with unique political twists. Lee talked a kind of social Darwinism: let the smart get rich. Yet community and business life were regulated in ways that made it hard to fall into the gutter. It sounded like rugged individualism, but felt like a welfare state.

To tourists, the paved and landscaped island can seem like one giant, hygienic shopping mall. But to foreigners who have worked there for a while, especially if they've also worked in the more picturesque surrounding countries, the rigid lack of corruption was itself almost exotic.

When I visited Jack Bradie, the head of the expansion project at the refinery that I was helping to finance, he was consulting with a young woman whom he'd brought from Britain to solve a sulfur problem. Sulfur is an impurity in crude oil that corrodes machinery, fouls catalysts, causes acid rain, and smells like rotten eggs. Singapore had just toughened its standards for sulfur in the air, and the refineries had to find new ways to get rid of it.

Jack was recounting his conversation with Singapore officials. "'We breathe here, too,'" he told them. "'But the equipment to process it cleanly will cost $30 million. What do you say?' They say, 'Hard luck.' Now, if we produced in a country with no environmental requirements, we could make you $30 million more." (Jack got a kick out of addressing me as the visiting financier.)

"Then why are we in Singapore?" I asked. Caltex was in Thailand to refine oil for that booming country's population of 70 million. But Singapore's population was only 3.5 mil-

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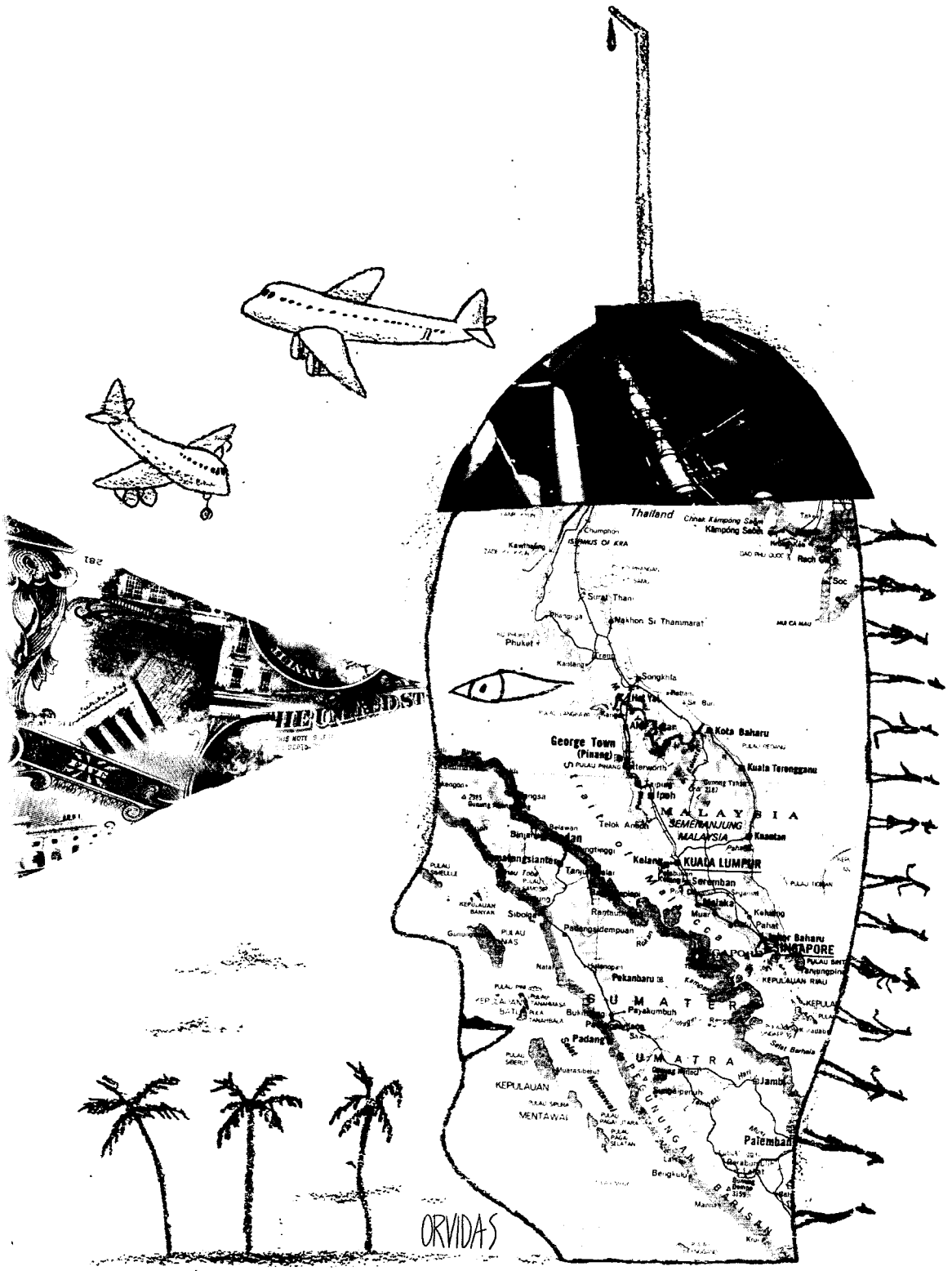

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lion. "They don't use oil, they don't produce oil, they have tough environmental standards, and there's no one to pay off."

"That's exactly why we're here," Jack responded.

Apparently other oil companies agreed, because Singapore had seven offshore islands set aside for the multinationals that chose Singapore as a place to process oil. And the refinery islands were so crowded that the government was expanding them through a landfill project.

One reason the companies don't move out when environmental regulations become more demanding is that Singapore's rules are reasonable. Another reason is the excellent infrastructure. The Singapore government had built a four-foot-wide pipeline to carry oil from out where big tankers could anchor, over to those refinery islands that didn't have deep harbors.

The fee was 5.5 cents a barrel. That's not cheap. But no one would ask for another penny. No one from Caltex Singapore would have to sit in a bureaucrat's waiting room for three months wondering what other oil companies offered for a permit to deepen the harbor, as happened during the course of refinery construction in Thailand. The Singapore pipeline was soundly built (not by someone's brother-in-law), and the costs were equitable for all the companies and could be calculated in advance.

Engineers like those who planned the Singapore pipeline could be hired by other governments in the region. But the discipline to choose the best, regardless of self-interest, and to administer the facility for the common good, was uniquely Singaporean. I asked Jack how he accounted for the quality of civil service.

"What happened in Singapore is Lee Kuan Yew," he answered without hesitation. "If they see any corruption they come down on it hard. It's not a cultural thing; it's a national decision that comes from the top! I feel lucky to work here."

HOW TO MAKE A REFINERY GO WHOLE HOG

You can think of petroleum refining like hog butchering. They hack the ribs off for chops, the belly for bacon, the thighs for ham, the guts for chitterlings, and grind the bones into fertilizer. Crude oil is a mixture of thousands of different compounds. Refining is a distilling process that separates the mixture into salable "cuts" (that's the term in the industry) like kerosene, naphtha, gasoline and diesel fuel. The cutting is done with heat. The crude oil is heated in huge processing vessels until its components boil off as vapor. Butane will vaporize at less than 90 degrees, gasoline between 90 and 220 degrees, various heating oils and diesel fuels between 450 and 800 degrees. Eventually we're left with residues so thick and heavy that they're used to pave roads.

But there's an important difference between meat and oil: some petroleum cuts can be changed into others. Using chemical catalysts at temperatures above 900 degrees, our new catalytic cracker would transform cheap, heavy residues into high-grade gasoline.

"Pigs' feet into pork chops?" I squeaked to Jack Bradie.

"Straw into gold, I'd say."

"So I've made a good loan."

"That depends on the price of gold."

Building a new refinery from scratch is unusual. But refinery upgrades are constant. Caltex Singapore had borrowed more than $300 million to pay for its part of the catalytic cracker under construction at the refinery that Caltex shared with British Petroleum and the Singapore Petroleum Company.

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Jack Bradie, that crusty/soft Scot, was director of the team building the cat cracker. His office was at the construction site on Pulau Merlimau, the island that housed the joint refinery called the Singapore Refining Company (SRC). But before I visited Jack on the island, I took the official tour.

THE GUIDED TOUR

Peter Foo, retired from the Caltex Singapore treasury department, was called back to guide me for the day. He was a tiny, lively man whose age was suggested only by his bowed legs and old-fogy opinions. Example:

"How do you like the Singapore subway?" he asked me.

Now, the Singapore subway is the eighth wonder of the world, so why not admit it? "It's glorious, Mr. Foo. Quiet, clean, perfectly air-conditioned."

"Not like the New York subway."

"Well it's older, of course, but..."

"Very dirty, I'm sorry to say. But you have your human rights."

He enumerated the right to litter, the right to chew gum, and the right to draw graffiti. That last right was the most controversial at the time, since Singapore had recently caned the backside of an American student convicted of recidivist graffitiism.

"Many Americans agree with Singapore on that," Mr. Foo assured me. "They want discipline." My noncommittal shrug evoked a Socratic dialogue on discipline that lasted throughout our drive across the island.

"You hear they say we hang someone too quickly?" Foo asked. "Same thing, you know, human rights."

He referred to foreign protests still swirling around the execution of a Filipino maid, Flor Concepcion, for a murder that her defenders suggested was committed by her Singapore employer.

"I'm sorry, I didn't follow the case."

"Also, you know Tiananmen Square?"

"Oh, yes. I did follow that."

"Students say they have human rights. Anyone can do anything. That's your human rights?"

Funny, this sympathy for the government of China. Foo's economic philosophy was hardly leftist. Here's a sample:

"Cars are expensive here. Where do all these people get money to buy them? The CPF [Central Provident Fund] is not working."

Every Singapore worker is required to put 20 percent of his or her salary into a Central Provident Fund, to be matched by employers. So at least 40 percent of all wages are saved for retirement. Under Lee Kuan Yew, the government had borrowed that money to build the homes in which most Singaporeans live.

"The CPF-forced saving is supposed to be anti-inflationary," Foo complained, "but banks have so much money they make loans to buy cars."

"Can you take money from your retirement fund to buy a car?" I asked. I knew Singaporeans could borrow from their funds to buy an apartment or to pay for education.

"No," Foo explained, "but the banks have so much money that now they want to make installment loans, and if the house is paid for out of a CPF loan, and the college, then you don't need the money each week so you buy a car. That defeats anti-inflationary purpose"

We reached the pier from which we caught the ferry to the refinery. At 9:45 a.m., there were about 40 men in short-sleeved white shirts on the boat. I made a note to come back here by myself at 6:30 some morning to watch the migrant construction workers going over. But it turned out that they used other piers less accessible to me.

On the short ferry ride, Mr. Foo pointed out an electric power station and two islands:

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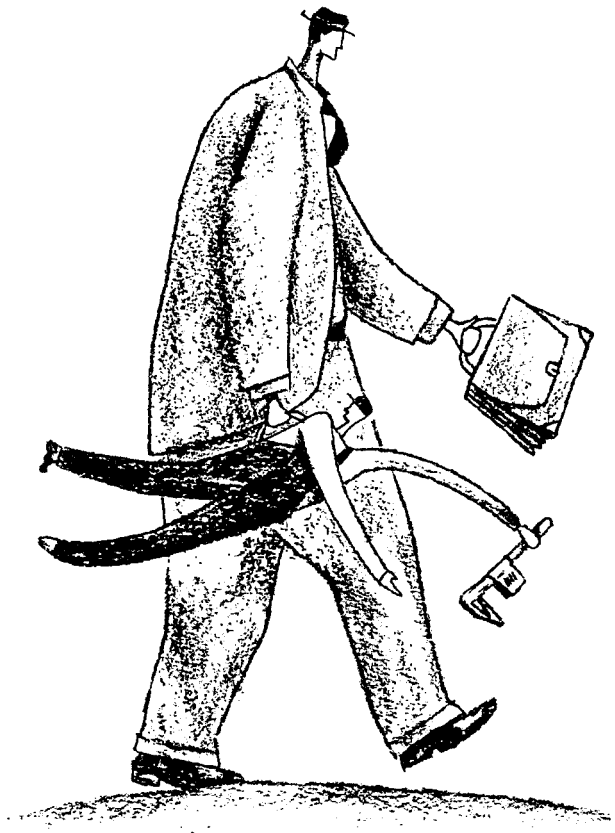

"Here's SRC. Next-door is Esso, the big boy."

"And what's that?" I asked, knowing that the pinkish hulk moored off our island had to be "the Love Boat," as it was called when it was used to house troops during the Gulf War. Now it was used as a dormitory for some of the migrants working on the catalytic cracker. There are eight official nationalities housed on the ship, and separate mess halls that serve Filipino, Burmese, Bangladeshi, Indian, Malaysian, Indonesian and two kinds of Chinese food.

"That's the floating hotel," Foo answered.

"Do you suppose I could visit it?"

"The hotel is not part of the tour. After this project, it's going to Thailand."

So in Singapore, the workers I wanted to interview were not only off limits, but also offshore. In fact doubly offshore, for they lived off the shore of the offshore island where they worked.

I surrendered my camera when we landed, and Mr. Foo helped me fill out my visitor's pass. Near the turnstile where employees swipe their ID cards, a warning sign said "Tempat Larangan" ("This Is a Protected Area"). It was also written in two Asian scripts and illustrated by the silhouette of a man firing a rifle into the head of another man, with the shot man falling backwards.

"Singapore security is very proactive," said a fellow with a walrus mustache and eyes he could roll the way the comedian Jerry Colonna does. "During the Gulf War, 100 soldiers were stationed on the island. It was a regular armed camp."

We were joined by the refinery's theatrical public relations man, Joe Fernandez. Mr. Fernandez, born and bred in Singapore, as he told me, was an East Indian. His Portuguese name probably came from Goa or Malacca.

"If you notice, there are four flags flying now: SPC, Caltex, BP, and the fourth, SRC. (The Singapore Refining Company flag had a blue triangle with a yellow oil drop.) During the war, the government said, 'Please take down the flags.' Reason: 'We don't want to tell any infiltrator we got British or American investment here. After the war, 'OK, you can fly your flags again.' Very proactive."

Even in peacetime, the photo I asked for – me next to the catalytic cracker – would require permission from all three refinery shareholders. "And Peter Foo would have to be rehired to come with you another day," Fernandez discouraged me. But the refinery's photographer would be happy to take my picture out here by the ferry. "Smile."

I'm so dumb that I actually thanked the man and gave him my address without realizing that he was there to take security photos,

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not souvenirs.

Formalities over, F&F rushed me into an over-air-conditioned conference room where Fernandez bombarded me with slides and statistics.

"SRC has 14 to 15 million Singapore dollars a month operating expenses, to be recovered in different proportions from the three shareholders. Last year, we paid Sing dollars 3.358 million interest cost."

"Mr. Fernandez..."

"Electricity 24, 25 million; pipeline fee, 5.5 cents a barrel..."

"I'm not actually here about..."

"Ferry 2.5 million each; water is supplied by Esso."

The word "water" seemed to arouse Foo. "As our prime minister – excuse me, senior minister – says, 'if you feel sick from drinking our potable water, you let us know, we'll give you medical care free.' Ha, ha."

"Okay [back to Fernandez], this is what the head count is like: 237 execs, 393 non-execs, for the RCC [my Residual Catalytic Cracker] we got 22."

"Twenty-two? What about that boat out there?"

"Laborers," he dismissed them. "The contract went to JGC [The Japanese Gas Company]. They got 4,200 workers at the peak of the project, 1,400 stay on the Habiba. It belongs to a shipyard. JGC leased it."

"These 4,000 workers are not allowed to go onto the mainland," Peter Foo said.

"People with work permits can be shuttled every day." Fernandez seemed to be contradicting Foo about the rules for migrants, but he smoothed it over. "It's all done by JGC. SRC doesn't want to know anything."

There we are again: "Not our workers."

"Mr. Fernandez, did anyone tell you I'm writing a book about the way my own money moves around the world? My bank happened to lend Caltex the money for the catalytic cracker. What I'm really interested in is..."

"Okay, I'm going to show you a video now, 'Cracking the Crude!' I'm sorry if I disappoint anyone," he said, taking the tape out of its box with a theatrical leer. "It's only blue on the outside."

He shoved in the tape.

"I don't think I need to see a videotape. Please. I don't do that kind of journalism."

But F&F were out the door before I could stop them. The music rose; it was the same heroic theme as "Raising the Column at Map Ta Phut." Twenty minutes of petroleum chemistry in a freezing room.

As it ended, they returned, bringing soft drinks, and Fernandez flashed a slide of shift schedules for the coming year. "In Singapore we have 11 public holidays..."

"Mr. Fernandez! I'm in Singapore for the residual catalytic cracker. I've come halfway around the world to see it."

"Presently there are 77 tanks on the island. The RCC will add another 19. The RCC will cost 1.4 billion – original estimate 1.3 billion. It will add 33,000 barrels per day and the accounting will become even more interesting."

He was right. Accounting between the rival petroleum companies was indeed interesting. Each of the three companies owns different shares of the facilities on the island. Caltex might own 41 percent of the crude distilling unit, British Petroleum 38 percent, and Singapore Petroleum Company the rest. They would own different shares of the completed catalytic cracker, too. Each of the three companies also sources its own oil. Caltex was the first American company to buy crude from Vietnam after the Vietnam War (which, in Southeast Asia, I heard called "the American War"). The Singapore Petroleum Company had been buying oil from China since early in

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that country's opening to capitalism. British Petroleum got a lot of its oil in the North Sea. And of course, each of the three competitors sold to its own customers.

As for Fernandez's direct employer, "SRC doesn't buy or sell any oil. Our three shareholders buy and sell and they come to us and say 'SRC, will you refine this for us?'"

Some weeks, British Petroleum may want a lot of naphtha and the Singapore Petroleum Company may want a lot of diesel fuel. Caltex may own 60 percent of the naphtha-producing facility while the Singapore Petroleum Company may have bought some crude, which contains a lot of naphtha. The oil, meanwhile, flows continuously. Who owes whom what?

"We've got a section called the oil-accounting section, which keeps track of the borrowing and lending. There's so many committees. There's 10 meeting rooms in just this building alone. You'll like the 'demurrage' committee." Fernandez used his eyes to put quotation marks around the word "demurrage." He knew I collected industry lingo.

"Demurrage," he explained, "is the money you pay for the idle time of a tanker. If we (SRC) say to Caltex, 'Okay, you can come at 11 and load asphalt,' but at 11 o'clock we are not ready, we pay demurrage. If a Caltex tanker comes in and a BP tanker is still occupying the berth, BP has to pay Caltex. There's plenty of cases of demurrage between the three shareholders, and we got a demurrage subcommittee."

These days computers make settling up easier. But like the bookkeeping between rival banks that lend each other hundreds of millions overnight with no security, electronic accounting between the oil companies replicates systems of trust and cooperation that go back to an era long before computers. I was amazed at how these international competitors cooperate at the top.

There was cooperative bookkeeping among oil employees at lower levels, too. Demurrage usually involves a miscalculation on someone's part. "If I owe you eight million in demurrage at the end of the month and you owe me six million," a not-to-be-named Asian engineer explained to me, "that's two million changing hands and a lot of waste to report to home offices. But if I owe you three million and you owe me one million, that's the same two million, but we each look better." So they modify the numbers proportionally. It's nice to see international cooperation among workers, too.

Unfortunately, it seemed to stop at that level. When I visited the three top officials of the United Workers of the Petroleum Industry, Salehan, Subramaniam and Song, they made it clear that they represent only Singaporeans. That triple-S leadership team, as well integrated as the precinct squad on a TV cop show in the United States (except no women), was a testimonial to Singapore's resolve to contain ethnic hostility. The governments of neighboring Malaysia and Indonesia had been rightly accused of exacerbating ethnic tensions, at times, to firm up their power.

The well-integrated union leaders described their employers' economic problems sympathetically, then they approvingly explained the tax system that requires Singapore employers to pay the government a monthly levy for each foreign worker. In some cases, the levy is as high as the foreign worker's salary.

"But that's a hundred percent tax on a very poor fellow worker," I said.

"But if it went to him, the money would go out of Singapore and wouldn't be part of our GDP," said one of the union leaders. The important thing, as the three struggled to make me understand, was that the wage and levy

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together be high enough that employers couldn't use foreigners to undermine the Singapore wage. What part of the money the migrant worker got paid was not a union concern.

None of these men had been a union leader before Lee Kuan Yew's tenure. That generation of trade unionists had been dispersed or jailed. That made it easier to offer Singapore as a low-wage haven in the early years of economic development. Those years coincided with the period in the early 1970s when Western manufacturing was moving abroad. In other words, it was the opening of what many called "the global era." A World Bank publication called "The East Asian Miracle" described the process, saying "Japan, Korea, Singapore, Taiwan, *restructured* [the emphasis is mine] unions to ensure political stability."

At a later stage of development, Lee Kuan Yew decided that low wages were subsidizing inefficient businesses and allowing Singapore firms to keep going without automating. To increase productivity at that stage, the government began to regulate in order to require higher wages. That policy was still in effect when I visited. These cooperative union leaders had never personally experienced a government push to lower wages.

Did I ever get to see my catalytic cracker on the tour? I'm not certain. We eventually drove around the refinery. If I assume that any construction in progress was connected with the catalytic cracker, then yes, some of the tanks and pipes that I drove past must have been constructed with the Chase loan. But they didn't make much of an impression.

I did get a closer look at the Love Boat. From the ferry, it had seemed pearly pink in the morning, but when we drove past at around noon it was a flat gunmetal gray. I didn't see any people on deck in the middle of the day, but I did see two shirts hung out to dry. From this medium distance I could imaging life aboard as anything from prisonlike to a World War II troop ship with Frank Sinatra, Gene Kelly and Jules Munshin set to come bounding off for shore leave.

The important thing, as the three struggled to make me understand, was that the wage and levy together be high enough that employers couldn't use foreigners to undermine the Singapore wage.

That's as close as I would have gotten to a refinery worker if it hadn't been for Jack Bradie. When I visited him in the director's office, Jack obligingly introduced me to the JGC personnel man. JGC was the primary contractor that hired the subcontractors that employed the manual workers who were raising the catalytic cracker. This interview should have brought me one step closer. But though the personnel man answered all my questions, I didn't learn a thing. Migrant labor is a sensitive subject in Singapore.

"Those questions," Jack said, "if you asked any subcontractor, they'd be suspicious." He could think of one possible exception: "a capable lady" who ran a shipping and construction firm that was doing some special-

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ized piping on the cracker. "Edna Ko is smart and charming, and no bigger than you."

I called Ms. Ko from Jack's office and we made an appointment for the day after next. (This wasn't the first time size-ism had worked in my favor.) In a large open office in a mixed business/light industrial mall, employees, in the background, work at drafting tables and computer screens.

Ms. Ko was as charming and as smart as reported, and straightforward, too. "Our contract on the RCC is for $17 million," she said as she led me from the reception area to her own small office.

"Ms. Ko, how did you get into such a specialized business?" I asked. It sounded embarrassingly close to "What's a pretty little gal like you doing with ships and oil pipes?"

"My father started the business – my late father. Our company basically does a certain portion of the job, engineering and piping, both fabrication and installation. My brother runs the Hong Kong office."

"It must be difficult to find labor here in Singapore," I said, approaching what I thought would be the sensitive area.

"We relied on Malaysian before," Ms. Ko answered matter-of-factly. "But because of that labor supply becoming depleted, or more difficult to source, or more [she searched momentarily for the word] more expensive, we can say, we have to go to non-traditional sources – Philippines, Bangladesh, mainland China."

"You actually go to China?"

"Let me get my chap who's the expert on that." She spoke into the intercom in Chinese.

A man with a crew cut, short-sleeved shirt, chinos with bulging pockets, and rubber-soled shoes appeared almost immediately. (Ms. Ko, by the way, had smooth bobbed hair, wore a fashionable unfitted suit jacket, a slightly flared skirt and flat heels, and had a Prada purse.) She explained to Mr. Goh, the Chinese manpower expert, that I came through the people at Pulau Merlimau and would like to understand the special problems of recruiting labor in Singapore.

Given the OK, Mr. Goh was off and enumerating faster than I could copy it down. "Quota, levy, security, testing. "

I gradually made sense out of a ream of regulations designed to control migrants and make sure they don't stay in Singapore, and administered (at least currently) to ensure that foreign labor doesn't undercut Singapore wages. Every request for migrant workers had to be approved by a government agency that examined Ms. Ko's contract with the oil company. Each industry is allowed so many foreigners per Singaporean employee. Mr. Goh's quota at the time was five to one, or, "One Singaporean is worth five foreign labor," as he put it. The workers may come from only specified source countries. "In present labor market," Goh explained, "we must go to NTSes [non-traditional sources], which means Thailand, Philippines, Burma, Sri Lanka, India, Bangladesh and, seventh, China is a separate category." (Workers from neighboring Malaysia, the "traditional source," can come and go more freely.)

In addition to salary, employers pay the levy, then $440 a month (in Singapore dollars) for unskilled workers, $200 for skilled. (Making unskilled workers as expensive as skilled workers was part of the policy of increasing productivity.)

Mr. Goh has his skilled workers pretested in their countries of origin to make sure that they can pass the exams they'll be given in Singapore. For most jobs, the tests would take half a day, but because of security and safety concerns at refineries, it might be two weeks before a pipe fitter received the photo ID that allowed him onto the island. Goh would try

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to find offsite tasks until then, but he couldn't become a labor contractor renting his workers out.

The company also puts up a security deposit of $5,000 per migrant, to be returned when the individual goes home.

"How much does this all cost you, Mr. Goh?"

"Unskilled, the pay might be $450 a month and the levy now $440, meal allowance $250, plus air ticket, insurance, accommodation and utilities in the accommodation."

"So all together, the monthly cost of a foreign worker?"

"Every job is different but a foreign welder costs about $2,500 a month."

"And how much would a Singapore welder cost?"

"Salary, 1,500, CPF," Mr. Goh did a quick calculation and came up with the same number: 2,500 Singapore dollars a month.

"I would like to use Singaporeans if I could find them but there are pros and cons. They are choosy." I was struck by that use of "choosy" because I'd just seen the word used the same way in a speech by Lee Kuan Yew scolding Singaporeans for refusing night-shift jobs. "They can just go off the job in a day, unlike... (Mr. Goh took a few photo IDs from his pocket) These people have no choice."

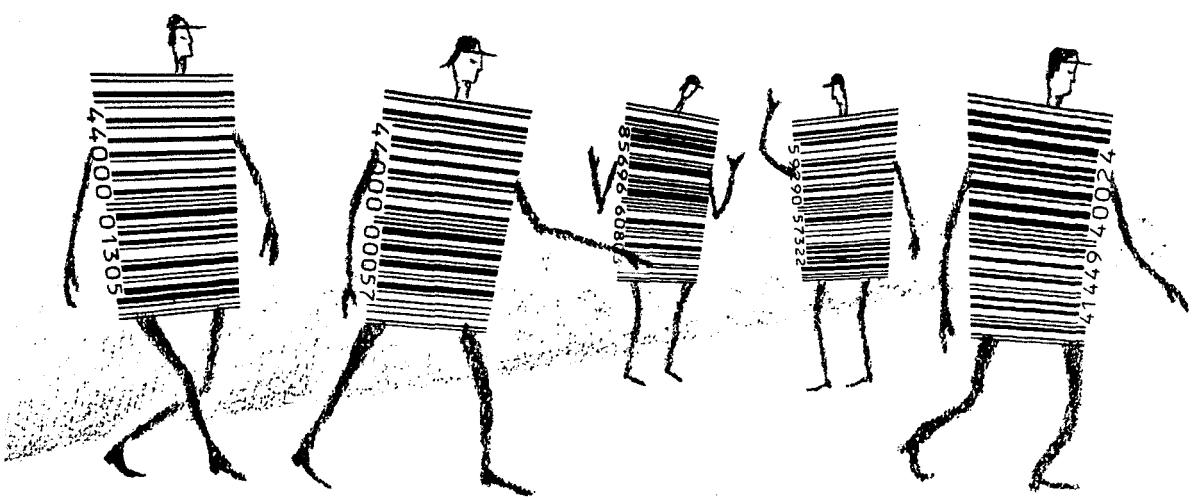
I picked up the ID of sad-eyed, mustachioed F. Pellegrino from the Philippines.

"Their passports are retained by us; their contracts are for two years." I wondered why Pellegrino's ID was at hand, but I didn't ask.

"If a Singaporean says 'I'm not coming anymore,'" Goh explains, "he will have to pay one month salary minus what's owed to him, or I go after him in small-claims court. But if a Filipino wants to go home, he will have to repay his air fare, buy his ticket home, and pay the company for two months if he worked six. If he frustrates his contract he will be held in detention till he is repatriated. But there's a disadvantage: I must keep paying his food, accommodations, and utilities at his accommodations, even if work stops."

It's the old debate: wage labor versus slave labor.

Mr. Goh gave me capsule descriptions of some of the migrant groups that he could choose from at the moment. "The Banglas are obedient. They feel committed because of the money they paid to come." Goh pays a local



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agent to find and screen workers, but workers also pay agents themselves. In Bangladesh it can cost a few thousand dollars to arrange a job, transportation and permits. Many rural people sell their land or go deeply into debt to send one family member abroad this way.

"The Bangladeshis are well behaved," Mr. Goh volunteered, "but some have very low IQs. They are peasants. Our Bangladeshis are all unskilled; no test required. They may not know how to read. I will talk to them in English and I will gauge whether they understand the language. I will look into the well build of the person."

"Hmmm?"

"Whether he's strong, well built, 25 to 33 is what I take. Just visually, if the guy is wearing glasses, I don't take people with glasses. The funny thing about the Banglas, they don't wear glasses. Either their eyes are very good or they can't afford glasses."

"And these Filipinos?" I was still holding Pellegrino's ID.

"The Filipinos are one of the best in terms of skills and ability to interpret the job, and they can speak English because the Americans have trained them up in Subic Bay [a former United States military base]. This man," Mr. Goh referred to the card in my hand, "has been with us six years. I am getting him a permanent pass. But I must cancel his temporary permit."

I turned the card idly. Mr. Goh must have thought I was examining it. "The traditional source [a Malaysian] has the same card but a different bar code."

Bar code? With a scanner, authorities could tell the legitimate bearer's nationality, work sites he was entitled to enter, etc. I was starting to realize how carefully the Singapore government categorizes and keeps track.

"Indians, I only have six now. I'll see how they work out."

"And the Thais?" I asked.

By making the employer responsible financially, the government made as certain as possible that migrant workers will go back home.

"No Thais!" Ms. Ko breaks in, looking up from her work. "They're rigid and not so cheap."

"I heard they were good welders," I suggested tentatively.

"We had 45 for the Mobil job two years ago – welders, fitters and riggers," she explains. "When we wanted to split the group up they want to be together, all 45."

"They're very fearful outside Thailand," I defended the unknown migrants. "And there was that sleeping death scare, a couple of years back."

"But they were willing to be split up for more money," Ms. Ko replies.

"Ah-ha," said I, "so they were negotiating."

"I don't know if you'd call it negotiating or demanding." Ms. Ko was reseeing it herself now, in her mind's eye. "They put down their tools. They are capable to form a mutiny. So we repatriated them."

"Sent them back?"

"The same morning."

"The same morning!"

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"Not so much of a problem," Mr. Goh explained, perhaps misinterpreting my amazement. "There're direct buses out of Singapore. You only have to ensure that he has boarded the transport and surrendered the work permit, and do a final exit permit in full. Your $5,000 security is jeopardized if the exit pass is not signed with proof he went directly to his country of origin."

Should any of his workers fail to leave the country as scheduled, the employer would have to come up with the $5,000 security money in cash and forfeit it. By making the employer responsible financially, the government made as certain as possible that migrant workers will go back home. And as we've seen, they also make the use of migrants as expensive as the use of Singapore workers. Singapore was serious both about controlling population flows and about making sure that illegal workers didn't undermine local wages.

I was used to the United States, where lowering wages had been bipartisan government policy for as long as I could remember. So despite periodic campaigns against illegal aliens, no United States administration seriously troubled the employers who hired them, and several government programs supplied low-paid legal immigrant gangs to employers like chicken processors and sugarcane growers. Of course in Singapore, if Lee Kuan Yew should decide at some point that it was in the national interest to lower wages, he could do so openly with little opposition.

"Do you normally have to see each worker out individually?" I asked.

The Thai mutiny was an abrasion Ms. Ko could still feel. "We tried to talk to them. One of them spoke a little English. We had a contract we had to comply with, we were already on a 44-hour-a-week basis, but if we have to go round the clock [she is talking to the Thais now] we can give you this much more. No... yes... no. The agent flew down from Bangkok. He is talking to them; we don't understand. We talked until 4 o'clock in the morning but he failed to reach an agreement."

Mr. Goh told me about a new labor source that promised more predictability.

"In China, we have recently made contact with a company that operates the same type of projects as ours. They have 100,000 workers broken into divisions, just like the army.

"We tell them we want 100 to 200 people, we give them the breakdown of the trades, we negotiate the salary we will pay. We give the company the mobilization fee of $200 per worker and they'll bring them in a group, a complete work team with a project manager who comes in from China as foreman, and their own middle managers and supervisors. Their team is like a sub-sub-subcontractor. But we will pay the worker directly by his own check and he will sign a contract with us." Hiring and paying each worker individually is a Singapore government requirement.

"Will the Chinese be coming soon?" I asked.

"They are already with us. Two hundred Chinese already work on the RCC."

"You mean I'm already paying them? What kind of people are they, Mr. Goh?"

"We have welders, pipe fitters. A Chinese welder I pay $700. But the other costs, ticket, accommodations...."

"But what are they like?"

"They are from two different divisions. In that country each division has 30,000 men."

"But is it an army? Are they..." free labor, I was thinking.

"The uniqueness is that they kept their families with them. There's a province set up by this company in China and the family lives together and has their schools, their culture."

"At one time, we thought the Chinese would be cheaper," Ms. Ko interjected, "but

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they are aware of the rates now and if they work in Singapore, they know what the local worker is getting."

At the time, there were said to be fewer than 100,000 Chinese laborers sending home remittances. (There were half a million Thais abroad in construction work alone.) So my 200 mainlanders were truly a part of a vanguard. Remittance money had been a crucial source of foreign currency for kick-starting Korean industrialization. Now my bank deposit, lent by Chase to Caltex and paid as wages to Ms. Ko's welders, was helping to build the new capitalist China. Should I be proud?

The interview was coming to an end, but my mind kept going back to one matter.

"I keep wondering what I would have decided about those Thais," I said to Ms. Ko. "I'm not the kind of person to say on principle 'You can't tell me what to do.' I'd want to know what it was going to cost me either way. Now, I could calculate what it would cost to replace them, but the problem you had was..."

"Exactly," Ko nodded in grateful agreement.

"Once you've got this indiscipline..."

"Exactly!" She jumped in. "Once you've got this indiscipline on the site, you don't know what other delays they'll cause or what other people will demand later." I probably would have done the same thing. Predictability is the sine qua non for fulfilling a contract. Still, employers, even those as poised and rational as Ms. Ko, can act irrationally when balked by workers.

I asked Ms. Ko if labor was her main cost. "No, our main cost is equipment – cranes, etc.," she explained. I wonder if a demand to renegotiate an equipment lease would evoke the same raw feeling as had the Thai "mutiny."

I was more determined than ever to interview one of my own migrants. The Thais still seemed the most exotic. (What had those mutineers really wanted?) But I couldn't talk to them at work, couldn't hang around their separate pier, and couldn't ride in the vans that took them to their dormitories. So I hired a Thai translator and went down to the only seedy mall in Singapore.

When you ask Singaporeans for directions to what's known as the "maids' mall," they nod and even smile. "Straight up Orchard road. You'll hear the chirp-chirp from outside." Despite Flor Concepcion's execution, no one seemed frightened of the thousands of Filipinos who alight at a particular downtown mall every Sunday. Nor did people seem to mind the hundreds of slim South Indian men who stood talking in the parking lot at the entrance of the Indian quarter. But when I asked directions to the Golden Mile, people said "The Thai mall? That's not really Singapore," or "Maybe you don't want to go there alone."

Construction workers are generally free only on Sunday, so I'd cased the Golden Mile the Sunday before, ostensibly to buy green papaya for a salad. Young men flanked the entrance ramp, oddly silent. Inside it was rundown and there was rock music on the loudspeakers. A few men at tables drank beer. Many more squatted or sat in circles on the floors, joking and eating peanuts. They tore up cartons for cardboard to sit on. Groups that had been there earlier had left spectral circles of cardboard and peanut shells. In Singapore, litter is shocking.

Nobody here bothered me as I crossed the ground floor, escalated to the supermarket, and picked out a papaya. Still, it was creepy to move among so many men, none of whom spoke English. I was relieved to chatter to the checkout clerk about how you shred a green papaya. (Are we the only women here, I

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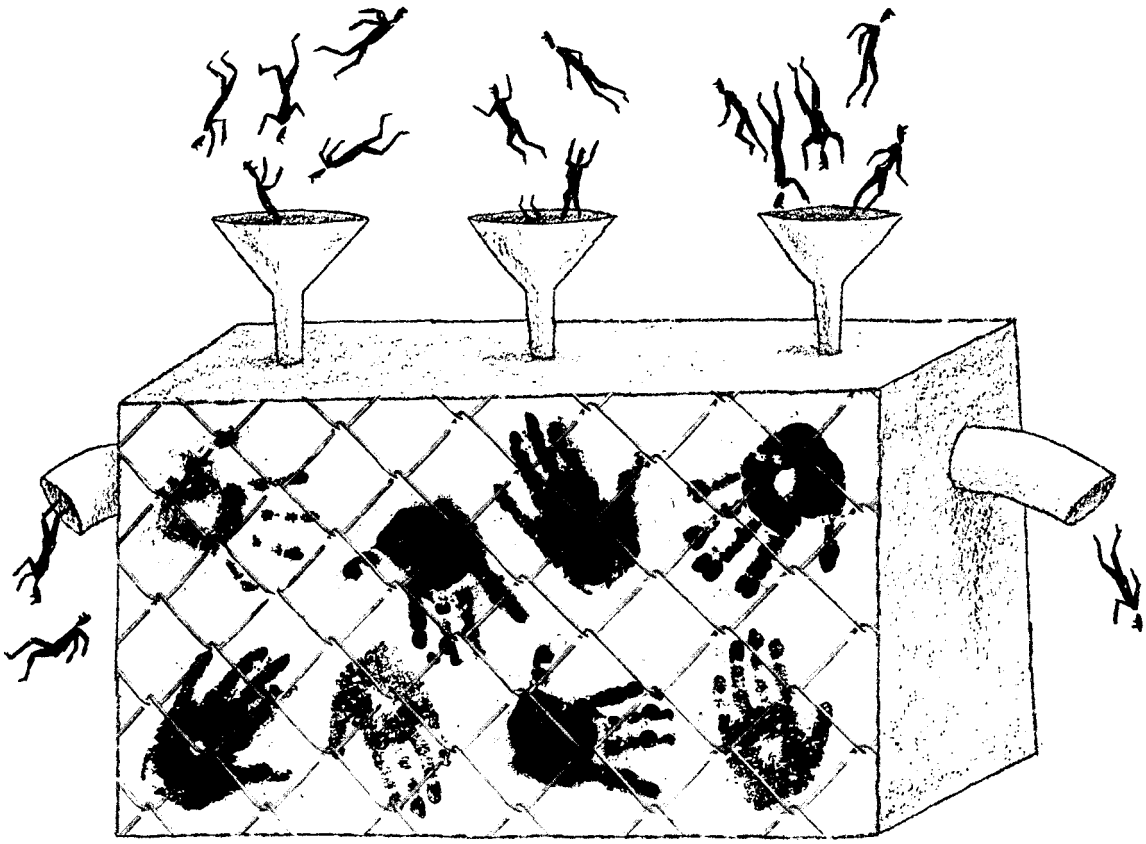

wondered?)

Now, back in the same supermarket with a translator, I noticed a young man engaged in intense conversation with an older woman. She was skinny and had to be almost 40. Look at the way they lean in toward each other, I thought.

"What are they talking about?" I directed the translator to the couple with my eyes.

"The health of someone from their village. She had to be brought to Bangkok to find a doctor. Either this one's his relative or the one they're talking about."

"Oh."

In an upstairs remittance shop, a sinewy old man thumbed through a sheaf of receipts. "I've sent home almost half a million baht and the wife says there's no money."

"How come?" I asked, already embroidering a drama of infidelity with a homecoming like Agamemnon's.

The man explained that he'd been a welder in Singapore for 11 years, and never missed a day's work. His company – Ferrenghis, which builds shopping plazas – gave him a big bonus after 10 years of about 80,000 baht. His wife had been buying land with his earnings and built a house on one of the plots. "We paid 200,000, now it's worth 400,000. But there's never any money."

The drama got less classical. Still, half a million of anything is a lot, even if it's only

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baht. And 11 years is more than half of Odysseus' voyage. The last time the man had been home was three years earlier.

"Does your wife ever visit you in Singapore?"

"The wife says she wants to, but I don't allow it. Letting her come to Bangkok is enough already. If she came here, there'd be no one to look after the children."

A second old man gave a supplementary explanation. "It's troublesome to get a passport for a woman. They say you want to be a prostitute. If a woman comes back from Japan, they take her to a room in the airport, and they say 'How much did you spend? What did you do? Who gave you that?'"

My translator confirmed this. "The last time I flew to Bangkok I saw a line of women outside that room."

Another old man wandered in to check the mailboxes. Once you've registered with a remittance shop, you can use it as a mail drop. The boxes here were labeled alphabetically; another shop arranged theirs by village. The man flipped through the mail to see who else was in Singapore. This seemed to be the old-timers' hangout.

Over in an electronics store, young men watched a kung fu movie, dubbed in Thai, on a large-screen TV. A magic warrior somersaulted up and backwards. The area of the floor where the men were allowed to sit was filled but not packed.

Downstairs, I bought a few pudsa (they look like tiny apples) from a man at a card table. He was originally from Northeast Thailand, he told me, but he was now based in Had-yai to make this trip every week. He'd gotten up at 4:30 that morning to peel 80 kilos of sour mangoes. "That's my sister." He pointed to a woman cooking fish balls in a large wok on the floor of a cosmetics booth, which they sublet on Sundays. "We have a regular Singapore sales permit. Business is pretty good."

There were also sit-down restaurants. On weekdays, the Golden Mile is a regular, though slightly shabby, mall where many Singaporeans come for Thai food. But the migrants seemed to make do with fruit, beer, fish balls and peanuts.

The place was getting to feel almost homey. At first I thought of remittance shops as akin to the pool halls and credit jewelers around American military bases. But I gradually began to see the Golden Mile as a useful, if not stimulating, community center.

A lively group of about eight men just finishing their business at a remittance shop invited us to sit outside with them in the alley. They bought bottled water from an old lady who ran after us with newspaper when she saw that I was going to sit down, too.

"There are benches across the way," I said, pointing into a housing estate. They indicated politely that perhaps they'd better not. "Singaporeans don't like to see us on the street," one said. I couldn't tell how much that bothered them. They were here "for the money." They each gave the same answer. Their stories were the same as a dozen and a half others I'd collected that day. Registered with an agent in town, paid 40,000 to 50,000 baht. Their jobs in Singapore: "Do cement." "Build flats." "Work in the shipyard." Everyone I asked was married. The money was sent back to wives and children.

"Are you married?" one man asked me flirtatiously.

"I have a daughter, 27!" I said with mock indignation.

Everyone laughed.

I found on this trip that any indication of my age turned unwanted interest into chivalrous solicitude.

"I'm thinking of finding a Singapore wife,"

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said the flirtatious one.

"Wouldn't it cost money to have a wife here?"

"Yes, I'd send less home than I'm sending now."

"I can tell you're not thinking that way," I said to a fellow I remembered later as round-faced with sandy-red hair and freckles. (Impossible, of course, but he was so visibly a country kid.)

"No, I've got two children. My wife is working in the paddy fields now with hired help [at 60 or 70 baht a day]. I'm not looking for a second wife." This was his second stint abroad.

Another had left his farm for the first time. "My wife will work it with the children and she'll hire people. This is the first time I've missed a harvest. It makes me feel very funny to think someone else is clearing the paddy." It was the farm that his parents and grandparents had worked.

"And your children?"

"I want them to go to school and work in government offices. I'll hire people to do the harvest when I'm old."

They had plenty of questions to ask me.

"What do construction workers get in America? How much did you pay for your ticket here? What about between Singapore and Thailand?"

Others had useful information, too.

"A couple of people from my village went to Israel. They take care of your food and lodging better than Singapore, from what I hear."

"When you go to Taiwan they will check whether you have worms in your stomach. Here they only check for fitness, but not worms."

"In Kuwait, the pay is better and you save it all; there's no place to go. You finish work and you sit in your air-conditioned room. They don't like Thais there." I've heard Indonesian women give similar reviews to Saudi Arabia. The reputation for having abusive or disdainful employers undoubtedly jacks up wages in those two countries.

"What about working in Thailand?" I asked.

"Plenty of jobs, but low wages."

"Even in Bangkok, the language and the low cost of living don't balance the high pay in Singapore."

"But in Bangkok," a plaintive young face mused, "when you miss your family it's reachable. In Singapore, you cannot just leave."

At the mall, I met only one Thai whom I'd call a hustler. He was handing out fliers for a new remittance shop. "The only remittance shop owned by a Thai," was his spiel. "Drop your remittance number into the glass bowl and win a thousand baht."

"Hello. You U.S.?" he asked me. It was the first English I'd heard at the Golden Mile. He wore slim-legged black pants and pointy-toed boots with stacked heels. His family still had a paddy farm in the north, but "farming in Thailand is old-fashioned and the reward for the money is no good." Years ago he'd been a trishaw driver. "I had a GI friend, Larry. I very much like Americans."

On his first trip to Singapore, Larry's friend had paid an agent the usual 40,000 baht. Now he was back on a tourist visa, picking up whatever work he could on his own. He was currently a building guard and also painted rooms for an interior decorator.

"And you do this, too," I indicated the leafleting.

"I'm just doing that for my friend. Friends do things for each other. If you do good, you get good. That's what they say in my family."

Until that moment, I hadn't connected the Southeast Asia I was visiting with the Southeast Asia of American GIs on R&R dur-

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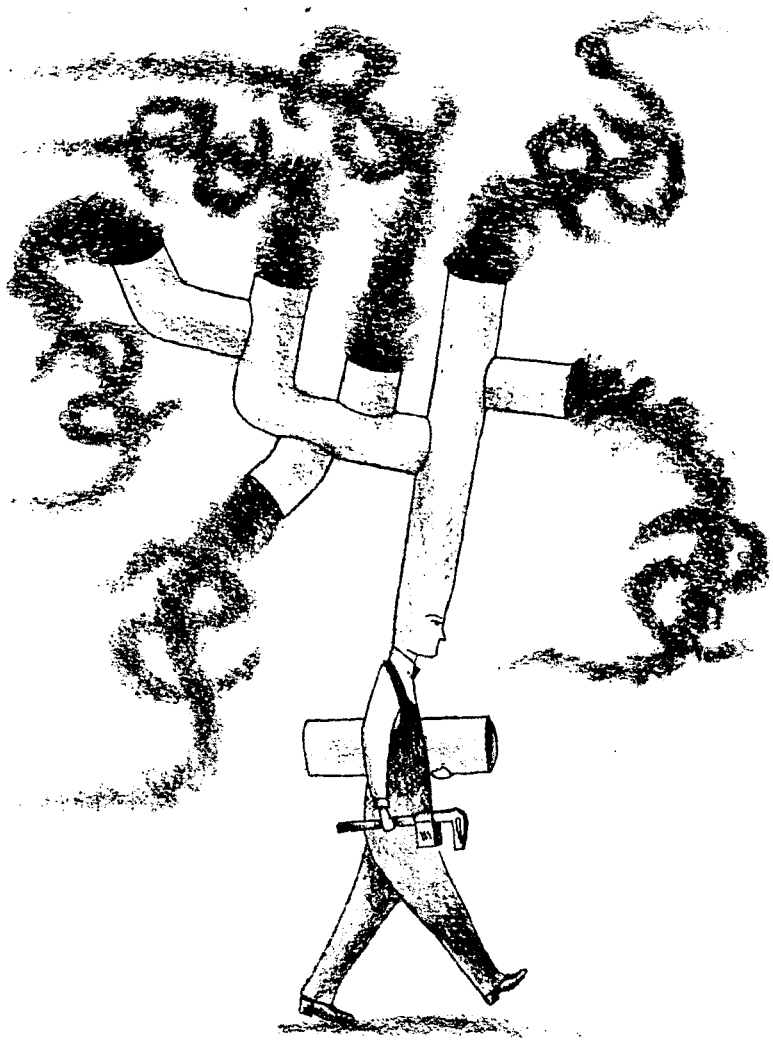

ing the Vietnam War. What happened to the hanger-on types when times changed? They're still here now, of course. Just as the decent and self-respecting were always there, then.

It was toward the end of the day when we sat down with three young men at a table against the wall, drinking beer (one bottle each) and looking bored or sad. Two were classically handsome Thais in T-shirts. The third had chipped front teeth, a plaid shirt, and a goofy center part that made him look like Alfalfa in "Our Gang."

All three had been brought from Nong Khai by their Thai agent and now lived on the premises of their Singapore contractor in corrugated metal containers, five people per container.

"I have a container with air con [air conditioning], refrigerator and TV in the common space," said Alfalfa. "You cook outside. Most of them have a window."

The shyest of the young men – "He doesn't talk to us either," the second-shyest explained – did unskilled construction work on new apartment buildings. The other two were pipe fitters sent out to different oil refineries.

"Oh, which refineries?" I was trying to

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sound casual.

Alfalfa fanned out a set of plastic IDs. Mobil. Esso. And there, with its blue triangle and yellow oil drop, was the card he swipes to get onto Pulau Merlimau. This man works for me!

I asked, as openendedly as I could, if there was anything he particularly disliked or liked about the refinery jobs.

"Sometimes I have to go to the factory to construct the piece [of pipe] that they need. Then I bring the piece back to the refinery and even though I did it according to the drawing and everything was correct, when I bring it back, sometimes it doesn't fit. This makes me fed up because I thought I could finish but now the job is not finished. I have to take it back and redo it."

"Will the foreman be angry at you?"

"No, he knows it's not my fault. "

"Some people would think it a nice break, then," I suggested, "to go back over instead of working in the sun."

"But I don't like to have to redo what I did. You feel so good when everything's right."

"Is there a part of the job you particularly like?"

"He likes it when the pipe has to fit with a 45 degree angle," said the translator. "He doesn't like the 90 degrees."

"What makes the 45 degree angle more interesting?"

"You have to think harder for the 45 degrees. If it's 90 degrees they tell you this length." He made an arrow. "It's straightforward. But if it's 45 degrees they only tell you this side. So I have to do some calculation. There is a formula," he added modestly.

"And you yourself do the figuring and the cutting and fitting?" I said appreciatively.

A warmth I could just about feel flooded his face.

"That is my ability," he said while looking down. "Yes."

All three of the young men came from a small city in northern Thailand near the Laotian boarder and expected to go back there. Here in Singapore they woke at about 6 a.m. "The boss [they used the phrase *tow kae*, Chinese boss] will come at about 7:15. There's a little excitement waiting for the foreman because we don't know to which place we'll be sent."

Because he'd had asthma attacks in Singapore, Alfalfa hoped he'd get to work outdoors, where there is less dust. "Also, to see the real thing is more interesting than just the drawing."

"Do you ever ask to be sent on one job and not another because of dust, say, or because you'd like to stay together with other Thais?"

"No," Alfalfa answered, "because you must respect the feeling of the foreman and what he needs to get the work finished." These were certainly not my Thai mutineers.

"Every day is routine work," said the quieter pipe fitter. "Only some days you wake up and think 'I am so far from home!' When you're sick in Thailand, other people will do for you – your family, your wife. But here you have to get water yourself if you're sick. "

All agreed that they missed family at home. Alfalfa's wife is a schoolteacher. "And we have a 9-year-old."

"But you look so young."

"I'm 28."

"You said that in English!" I had already written it down when I realized.

"I'm 28," he repeated. But he was embarrassed and would not attempt to say anything else in English.

Alfalfa had been in Singapore for a year, and planned to stay only one more. The original contract was for four years, but it was renegotiable after two. "Now that I have the money, I want to continue studying in

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Thailand."

"Will you stay in the construction field?"

"No, I don't think so."

Thai migrants who make it to Singapore tend to be the best-educated people in their regions. The remittances they and other migrants send home constitute over 50 percent of the income in some provinces. You can tell a village with good migration connections not only by the TV antennas on bamboo houses that journalists find so ironic, but by pickup trucks, fish ponds, and irrigation and other agricultural improvements. But few of the returning workers will contribute the methods they learned abroad to the Thai construction industry. You can't blame them for trying to get out of construction work, especially Alfalfa, with his asthma. But the sorry state of Thai education and economic planning meant that more courses wouldn't necessarily prepare him for a better job at home.

"By the way, you know that boat off the SRC island?" They all knew the Love Boat. "Do you suppose it makes people seasick to live there?" I fished.

Alfalfa actually knew someone who had lived on the boat. "He never complained about the rolling or anything." No, he couldn't introduce me to his friend. "He's gone from Singapore a month already."

I knew it was pushing to ask about another worker. And it's possible that Alfalfa was being politely evasive. But it's more likely that his Love Boat acquaintance was indeed gone from Singapore. Migrant life is migratory. The people you meet get transferred or go home.

THE MAIDS' MALL, LUCK PLAZA, ORCHARD ROAD, SINGAPORE

The following Sunday I went to the maids' mall, but without a translator. I was not lucky enough to run into a Filipino who just happened to work for a Caltex executive. But I had a nice chat with four friends who asked me to snap their picture together, first in front of the Kmart, then outside on Orchard Road. Though they had been neighbors on a small island and had signed with the same agent to go abroad, this meeting of all four in Singapore had been difficult to arrange because maids only get one Sunday off each month.

Three of the women worked for Singaporeans. "My Mister is an American," said the fourth. Everyone agreed that she had the best deal.

All four had left their own children and come to Singapore "for the money." Their families had decided that this was a good investment and pooled their savings to pay the agent's fee. One woman's family had borrowed the money. She was aware that they risked a crippling debt if for any reason she didn't finish her contract.

As part of their investment, family members, including husbands in three cases, had agreed to take care of the children. The one single woman was worried, however, because her sister, her children's chief caregiver, was getting remarried. She feared that her 14-year-old son and his new uncle would get in each other's way, and that her sister, with a new husband on the scene, couldn't give the younger children enough attention.

I asked lamely if the women missed their children. "Yes, very much," they all said. They couldn't seem to express it any better.

"I miss my children but I also take care of children here," said the woman with the teenage son. "The little boy I take care of was always frightened and crying when I first came. His mother says, 'If you aren't good, the policeman will come!' or 'Auntie broke her leg because you spit.'"

Guilt evocation must be popular with

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Singapore parents, because the other women chimed in quickly with their own examples: "The lights went out because you were crying." "The train is not coming because the train man knows you are standing in front of the yellow line."

"I think the little boy is not so frightened now," said the woman who was worried about her own son.

"Then you must be a very good nanny."

"Thank you." She smiled unhappily. "But I will be glad when I can go home because here I am doing it just for the money."

These women can only enter the cash economy if they have a product that can be exchanged for money. But child care for cash seems stranger to them (and to me, too) than pipe fitting for cash. In fact, it seems almost illicit. Telling a woman that she does it well for strangers is not as welcome a compliment as telling Alfalfa he pipe-fits well for many different oil companies.

Bankers often talk as though they create things through their loans, when in fact they merely turn money into more money. Their vanity in taking credit for the product had sometimes annoyed me, but the opposite humble error disturbed me more. Could a child survive if his caregiver wasn't doing many, many things beyond her contractual job?

"It's too bad you have to come all the way to Singapore," I said. "There must be houses to clean and children to take care of in the Philippines."

"Our own," said one.

"But the money is in Singapore," said the second.

"It is like the nurses," said the woman with the teenage son. "People from home study to be nurses and they will go to New York. But there are lots of sick people on our island."

"Yes, but the money is in New York," her friend reminded us.

Right, I thought, some of it mine. But how does that determine whose children get minded and which sick get nursed? Sometimes I understand this money trail, and other times I lose the thread and the results make no sense at all.

UNUSUAL PATHS

Migration routes, I was beginning to realize, don't run from nation to nation. They go from three towns in a rural district to three or four blocks in a distant metropolis, or from a particular island in the Philippines to a particular mall in Singapore. Legal or illegal, skilled or unskilled, migrant workers don't swarm over borders on speculation. They travel on marked paths to specific jobs. While I was in Asia, the indomitable Mr. Goh, using money that went from Chase to Caltex to Ms. Ko's company, was opening just such a pathway between Singapore and a province in southern China. But the path won't look like his blueprint for long. The migrants will modify it.

Chinese workers may be drawn to Singapore by my money, but they don't stream along like iron filings in magnetic lines of force. After all, the mainlander can speak to a Singaporean in his own dialect, he can also read *The Straits Times*, *The Asian Wall Street Journal* or a San Francisco comic book. He soon knows, as Ms. Ko pointed out, what the local worker is getting.

That Chinese welder will report home not only on Singapore salaries, but also on how he was treated, on where to get a good bowl of noodles, on new welding techniques, and on matters that I can't begin to imagine. Ants, and even iron fillings, modify the paths they move along. Human beings make changes that are unpredictable before they happen, but have a way of seeming obvious and even

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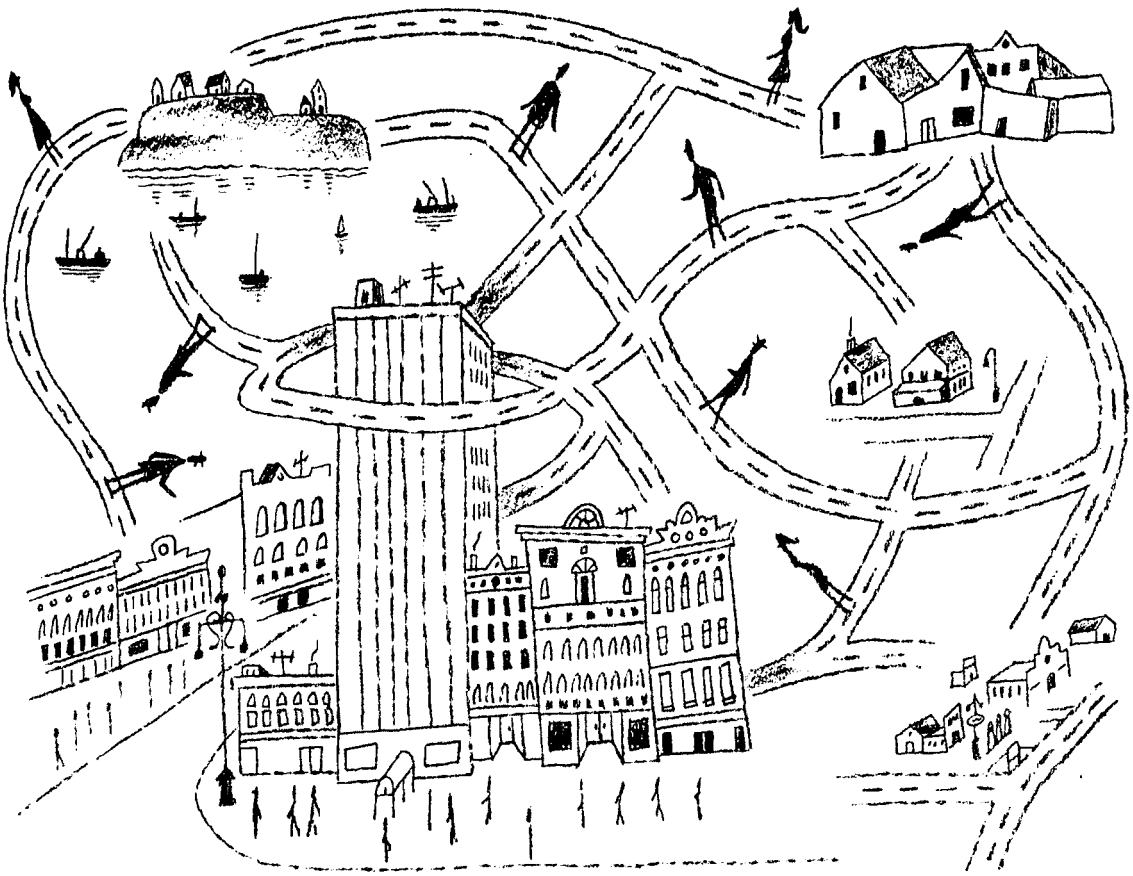

traditional as soon as they're in place.

My money, loaned through Chase, attracted rural Indonesians to Malaysia, where they built and tended shrimp farms, and it attracted Northeastern Thais to refineries in an industrial park south of Bangkok and in the city of Singapore. The migrants will take many things besides money home from these places. And despite all of Lee Kuan Yew's precautions, they'll leave more behind than the structures they were hired to build.

STYLES OF CORRUPTION

Before I left Asia, I learned how Caltex got the permit for its refinery in Thailand. The story involved both Thai-style and United States-style corruption. It would have been handled somewhat differently in Malaysia or Indonesia. It wouldn't have happened at all in Singapore.

Thailand has no oil of its own. Oil companies import crude oil and refine it there for the domestic market. Before the new Shell and Caltex refineries went up, the country had three oil refineries. In response to the booming economy, the Thai National Energy Policy Committee decided to issue a permit for a fourth refinery, and Shell won the bidding with its plan for a refinery at Map Ta Phut. But Caltex had already acquired all the

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land it needed while Shell was still shopping.

The Thai National Energy Policy Committee, seconded by the World Bank, was adamant in its decision that the country needed only four refineries. A fifth would destroy fishing and farmland for no good reason. As a kind of booby prize, the Thais ordered Shell to offer Caltex a 15 percent share in the new fourth refinery. That wasn't acceptable to either oil company.

Then suddenly the Thai government reversed itself and offered Caltex a permit for a fifth refinery without even opening bids. That seemed strange, since people knew that the Kuwait Petroleum Corporation was still contending for a permit. If a fifth refinery was now desirable, why not let everyone bid?

According to the *Far Eastern Economic Review*, the decision was taken by the Thai prime minister, and a small group of senior ministers, following lobbying efforts that involved the United States ambassador as well as senior Caltex executives. To justify their reversal, Thai government officials said that awarding the permit to Caltex was a tradeoff to get the United States to accept more Thai textile imports, and to ease its pressure on Thailand to open its markets to foreign cigarettes and to protect intellectual property rights. In other words, in exchange for a fifth refinery permit, there would be more textile jobs, fewer imported cigarettes, and cheaper pirated videotapes in Bangkok. The officials tried to present their switch as part of the give-and-take of ongoing trade talks.

Ignoring that explanation, Bangkok reporters jumped on the fact that one of the senior ministers involved in the policy change had a son-in-law who worked for Caltex. At the risk of sounding naïve, I honestly don't know how much – or even if – the son-in-law affected the permit negotiations.

While no Thai official justified the fifth refinery in terms of sound energy policy, it's still possible that the permit was based on other Thai national interests. It's harder to imagine the public interest that induced a United States administration to have its ambassador bargain away American textile jobs, cigarette sales and entertainment royalties in exchange for one company's right to build a refinery overseas.

Based on traditional styles of corruption, Thais assumed that the decision was made, on their side, for the sake of personal enrichment, while I, as an American, assumed that my representatives were moved to action by campaign contributions. Perhaps the main sense in which Caltex and its parent companies, Chevron and Texaco, are American multinationals is that they make their ongoing contributions to American politicians.

It's also possible that global-era politicians so honestly believe that what's good for their multinationals abroad is so good for the country that they would send in the ambassador, with or without specific linked contributions. That may be more insidious.

Whatever factor tipped the permit decision in Caltex's favor, who can say whether some of my bank deposit went into a Thai minister's son-in-law's salary, and some went into political campaign funds in the United States.

This is not to say that Caltex uses my money to spread corruption. Many kinds of corruption, particularly those most common in poor countries, are an impediment to day-to-day business operations. Companies like Caltex often help to clean up corruption on those levels. Julius Tahija, an Indonesian who was the head of Caltex Pacific Indonesia for 10 years, feels that "the promoting of an ethical business culture" is the most important benefit that a transnational like Caltex brings to his country. In a *Harvard Business Review*

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article, Tahija says "a stranger once approached me at Jakarta's airport, introduced himself as a businessman, and said, 'Something is wrong at Caltex.... Your accounting department is delaying payment to people to whom the company owes money. Unless people pay bribes, they do not get what's due to them.' I knew that this kind of extortion happened in some government offices. Even schoolteachers may have to pay bribes in order to get their salaries, but such a thing at Caltex was inconceivable to me." Tahija investigated and discovered that it was true: "After taking severe disciplinary measures, I distributed notices to our suppliers and contractors that anyone not paid in two weeks should call me directly at home. The problem disappeared."

"Honesty and dishonesty do not mean different things in different countries," Tahija says flatly. Furthermore, "ethical conduct is in a transnational's best interest."

What would happen if government officials and the public began to believe that a company such as Caltex made payoffs? Or that Caltex responded favorably to bribes? Or that the company kept two sets of books to hide income from local taxation? Every story of a payoff would stimulate requests for more. The government would continually renegotiate contracts in an attempt to get its share of hidden income.

And "contributions," whether directly or subtly requested, will win only temporary friends. When your payments stop, everyone's door slams shut. Once you buy a politician, the demands only grow.

Tahija insists that Caltex did not make payoffs, and I believe him. But he certainly understood the temptation. A common rationalization at all levels of corporate responsibility runs like this: It's ethical to pay government officials to do things they would normally do to discharge their duties, but it's unethical to pay someone to break the law. By this standard, paying a customs official to pass illegal goods is unethical, but paying that same official to expedite your shipment is all right. Such rationalization is tempting when your request for a building permit is at the bottom of the stack. Caltex often needed building permits. In Thailand, Joe Bartlett, the American who helped buy the land for the refinery at Map Ta Phut, also had the job of getting building permits from local officials. I asked him how you do that.

"You go to an office and say 'I'm trying to build a refinery.' They keep you waiting. There's no one to see. You just keep coming back till finally someone says 'Send us the paperwork.' What paperwork, what information? What do they want to know?"

"Maybe you were supposed to pay someone off," I suggested.

"We didn't."

"So what did you do?"

"I came back and sat in that office for about three months. I asked other companies what information they sent to get permits."

In Singapore, the government-channeled flow of money meant that "choosy" workers could reject night shifts and still live in modern apartments with electricity and running water, and that entrepreneurs could get rich by importing maids and building malls that catered to the poorest Thai migrants.

Of course, in all three countries, there was ecological damage and physical injury, and some people who couldn't take advantage of the new choices. They must have felt, and in many cases actually were, poorer than ever. But that was mostly in the hinterlands. Wherever my money flowed, there were new choices and opportunities. When I left Asia, they were playing musical chairs with more chairs than people.

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BY JEFFREY A. MIRON

Public institutions of higher learning loom large in American education. Almost half of the nation's 4,000 colleges and universities – schools ranging from community colleges to world-class research institutions – are government owned and operated. And almost 80 percent of America's 14 million post-secondary students are enrolled in public institutions, at an annual cost to taxpayers exceeding $50 billion.

Yet the desirability of delivering higher education through government agencies is rarely questioned, even when public primary and secondary education are under substantial scrutiny and the newly elected President is championing experiments in voucher privatization. This is not to say public higher education is immune from controversy; it is the scene of divisive skirmishes in contemporary politics, a battleground for affirmative action and the mores of political correctness. But for all the rancor, few question the notion that, with public higher education, more is necessarily better.

I think a debate on precisely this question is overdue.

The economic and social justifications for subsidizing higher education are far less convincing than is commonly assumed. Even if one believes that public money should buy a college education for every high school graduate willing to put in the time, it makes more sense to subsidize students at privately owned institutions.

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THE CASE FOR SUBSIDIES

It is the conventional wisdom that education benefits society at large, not just the people who end up with the sheepskins. For along with enhancing graduates' earnings potential and quality of life, education creates law-abiding citizens who are more respectful of democracy. By the same token, a better educated citizenry means higher productivity, more sophisticated culture, and so forth. Because the individual who obtains the degree does not capture its full benefits, the private incentives to acquire education are inadequate from society's perspective.

The view that education has beneficial spillovers certainly contains a kernel of truth. This does not mean, though, that more is always better – or that arbitrarily large subsidies for education represent good policy. To see why, one must simply recognize that education has costs. They include the direct costs of providing educational services and the opportunity cost of time spent obtaining this

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education (the income students could have earned had they not been in school). These costs can easily exceed the value of the education to the students or to society in general.

The critical question is under what conditions the beneficial spillovers from additional education justify the costs borne by taxpayers. And while there's plenty to argue about here, these spillovers, relative to costs, are likely to decline with the level of education.

Here's why. The spillovers from basic education are likely large. It's plain that societies function more efficiently if most members read and write the same language and accept common rules of behavior and conflict resolution. At the same time, the opportunity costs of being in school are low for primary-school-age children, and the direct costs of primary and secondary education are modest compared to the cost of college. Thus, the social benefits of education may far exceed the private benefits at the primary or even secondary level.

By contrast, the spillovers from college and post-graduate education are less obvious; the bulk of the benefit, in the form of income from specialized skills, is likely to be captured privately. It's true that liberal arts training is less directed at preparation for a specific occupation, but the spillovers from studying Shakespeare are less compelling than the spillovers from learning to count or read ballot instructions. In any event, training at this level comes on top of primary and secondary education; college students have, in principle, already been introduced to the humanities, science and the arts. None of this proves that higher education generates minimal spillovers. But the arguments suggest caution in using spillovers to justify subsidies.

Credit Constraints. Some people who could benefit from education are unable to afford the outlay, even though the additional income they could subsequently earn would be sufficient to cover the investment. Borrowing to pay for college makes sense here, but private lenders often refuse loans when the only collateral offered is the borrower's future income. Thus, government policies that make education cheaper – and thereby reduce the bite of credit constraints – can mitigate this market failure by raising output.

The spillovers from studying Shakespeare are less compelling than the spillovers from learning to count or read ballot instructions.

Even though there are people for whom the gains from education exceed the costs but who cannot afford the expenditure or borrow the necessary funds, the magnitude of this problem is easily overstated, since even the poor can often find ways around borrowing constraints. Academically qualified students can obtain scholarships or loans from private colleges. Those who cannot afford four years of classes can acquire education in smaller bites – night school, summer school, alternate semesters and the like – while earning income. And others can acquire skills by working at apprenticeships or attending school at an employer's expense.

Like the spillover argument, the credit constraint justification for subsidies is more

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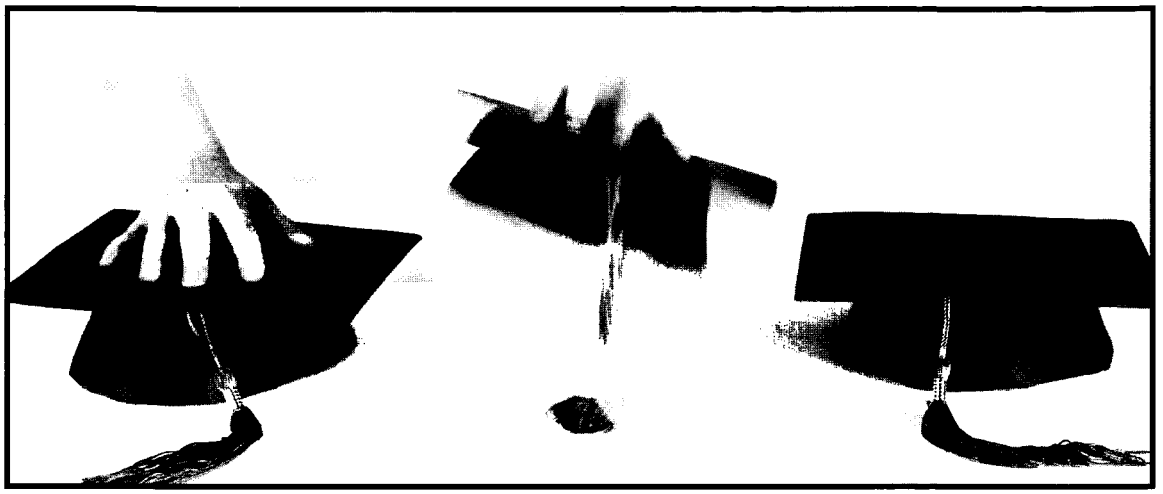

KEN BURRIS (ALL)

compelling when applied to primary or secondary education than to higher education. A five-year-old has few opportunities to earn income or to work as an apprentice, and few lenders are willing to wait decades for their money back or chase deadbeat debtors around the country. Again, the standard argument provides an uncertain case for government subsidy of higher education.

Subsidizing Education Versus Subsidizing Schools. Whatever their validity, the standard arguments for subsidy concern the demand for education; they are reasons consumers might purchase less than the socially desirable amount. An alternative justification for government subsidy might be that the private sector does not supply a sufficient quantity of education services.

For example, private markets potentially undersupply commodities produced under conditions of increasing returns to scale (e.g., local telephone service, if it were not regulated); such markets are typically dominated by a monopolist who restricts output to increase price. Even competitive markets can undersupply goods when there are information asymmetries between suppliers and demanders. Think of an insurance company that knows less about your health than you do, and thus charges a higher premium to cover the probability you are concealing an expensive medical condition.

But the supply-side rationale for government intervention is not relevant to higher education. Private colleges and universities thrive, in many cases outcompeting public schools. The plausible arguments for subsidizing higher education suggest, at most, that the amount demanded in the absence of subsidies might be insufficient; they do not suggest the public sector need supply those services that are demanded.

THE CASE AGAINST SUBSIDIZED SCHOOLS

Assuming that some degree of subsidy for higher education is desirable, the question remains what form it should take. Most public money today goes to government enterprises that supply higher education at tuition substantially below cost. Yet even a casual look at the consequences suggests serious problems.

Who gets subsidized? As currently operated, public colleges and universities distribute benefits in an arbitrary, even perverse, man-

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ner. They charge tuition substantially below the level of comparable private institutions, regardless of the financial circumstances of their students. And since most state appropriations for public colleges come from general revenues, low- and middle-income taxpayers underwrite the costs of educating students from high-income households. (Where states tap other revenue sources, the distributional consequences can be yet more perverse: Georgia's much-acclaimed Hope Scholarship program uses lottery profits, largely collected from the poor, to finance college for all high school graduates.) By the same token, middle-income households with few children or with children attending private schools are required to pay for benefits that go to the children of their peers.

The magnitude of this money shuffle is substantial. For the 1997-1998 academic year, the average tuition and fees were $3,110 at four-year public institutions but $13,392 at four-year private institutions. This comparison overstates the true difference if privates are higher quality than publics or if privates discount tuition – that is, provide scholarships – to a greater degree. But publics compete successfully with privates in many cases, suggesting quality is not dramatically different. And even at an average discount of 30 percent, private tuition is roughly triple the public rate. The difference, of course, is $50 billion-plus in state subsidies.

Public colleges and universities could rectify the distribution problem by switching to need-based tuition: a high, official tuition combined with discounts/scholarships that depend on financial circumstances. Other thing being equal, this policy change would be desirable. But if public colleges and universities reform by becoming more like private ones, they are, at best, doing something the private sector could do on its own.

Polarizing Policies. A subtler but nevertheless disturbing consequence of public higher education is putting government in the middle of America's culture wars. A prime example is affirmative action in admissions. In California, a ballot initiative banning affirmative action in state government, including in the operation of public education, was approved in November 1996 and became law in 1997 after surviving a challenge to its constitutionality. A decision by a federal appeals court in 1996 outlawed affirmative action in public colleges. The ruling applies in Texas, Louisiana and Mississippi. More recently, Florida's governor, Jeb Bush, announced a plan under which state universities would end affirmative action in admissions and instead guarantee enrollment at a state university to all students graduating in the top fifth of their high school classes – an approach already being used in states where affirmative action has been successfully challenged.

Any institution of higher education must take a position on affirmative action, so the potential for the divisiveness that issue can cause is present at both private and public institutions. But the potential for controversy is greater at publics, because government is the decision maker and because taxpayer funds support these institutions. Public institutions that do not practice affirmative action face charges of discrimination; those that do face criticism and legal challenges for engaging in reverse discrimination. Private institutions have more leeway to practice affirmative action, and many do so; few would challenge the right of a private institution to practice affirmative action.

Or consider divisions brewing around limits on academic freedom. At any institution, the presence of controversial faculty engenders a difficult trade-off. Sanctioning out-

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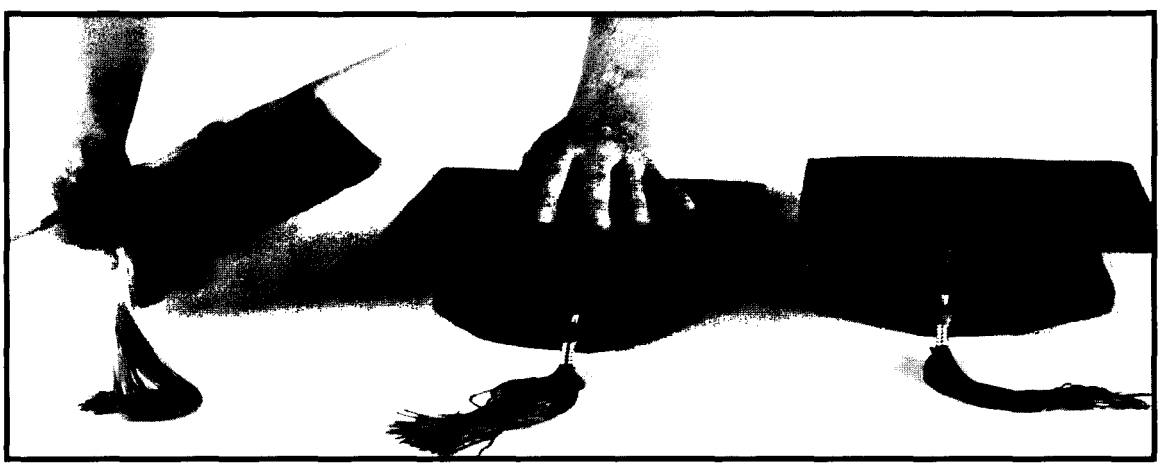
landish views might stifle the atmosphere of lively debate and free expression that institutions of higher learning value, yet tolerating such views can anger students, faculty and alumni. Private institutions can balance these considerations as they see fit, and there is scope for both variety and subtlety in their responses. Public institutions that must compete with privates value this flexibility as well, yet publics, as government entities, run afoul of constitutional free speech considerations that do not affect private universities if they sanction faculty members with unpopular views. Yet, the public institutions face more pressure than the privates to sanction views that are considered odious to significant portions of the electorate. Thus, at the publics there is no easy resolution of this difficulty.

For example, the City College of New York, a public institution, removed Leonard Jeffries as chairman of the Black Studies Department because he publicly asserted that Jews had helped finance the slave trade. Jeffries argued unsuccessfully in court that the school had violated his First Amendment rights. A similar controversy broke out at Wellesley College when three Jewish students discovered that Tony Martin, a professor of Africana Studies, had assigned a book suggesting Jews played a role in the slave trade. And Arthur Butz, a tenured professor of engineering at Northwestern, uses a university Web site to promote his view that the Holocaust did not occur.

Gender equality has almost as much potential for breeding division in publics. Witness the circus surrounding The Citadel and Virginia Military Institute, male-only public institutions that were forced to open their doors to women after the Supreme Court ruled that their exclusion violated the 14th Amendment. Here again, privates can more easily balance the pros and cons of single-sex education; few Americans wish to prohibit private, single-sex institutions.



Centralization, Standardization and Innovation. Every institution of higher learning must decide what programs to support, which faculty to hire, whether to emphasize teaching or research, and so forth. The decisions made by private institutions must meet the test of the market; those schools cannot impose a particular view unless consumers and donors are willing to tolerate it. But private institutions need not bow to the political considerations that accompany government funding.

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THINKING BIG

The decision makers who control public education, by contrast, are creatures of legislatures. Thus, the will of the majority in everything from curricula to sports policies is more easily imposed on public systems, and politically unpopular subjects or programs are more easily terminated.

This is especially problematic because public institutions set precedents that affect market perceptions of what constitutes a university. The effect is small so long as higher education is decentralized; in the United States each state competes against 49 other states, and all states compete against a vigorous private sector. But as public higher education expands, as has occurred over the past century, the practices of publics determine what the citizenry expects colleges and universities to be – thereby shaping not only public institutions but private ones as well.

Efficiency. A final disadvantage of public colleges is that they operate less efficiently than privates. All institutions of higher learning must compete for students, faculty, grants and donations. They therefore face competitive pressure to operate efficiently, even though they are nonprofit. But private institutions face these pressures to a greater degree than publics, since those that fail to control costs or offer an attractive product have no recourse to state funds. Likewise, private institutions have a greater incentive than publics to oppose regulation or collective action that raises costs. This means, for example, that publics are more willing to accept unionized faculty and staff.

This efficiency advantage of privates is difficult to measure – and is not necessarily large in the United States, where publics face substantial competition. Moreover, the fact that privates operate more efficiently does not guarantee a marked advantage in the quality of education, merely a better relation between quality and cost. These caveats aside, the efficiency advantage favors private institutions.

THE CASE FOR COLLEGE VOUCHERS

Despite the negatives of public higher education, there is still a case for government subsidy if spillovers and credit constraints are important. But there are alternatives to delivering subsidies through government-operated schools. The most obvious is vouchers. Under a voucher program, government pays part or all of the tuition for eligible students at private institutions. The eligible group might be high school graduates who have gained acceptance at an accredited institution. This approach is not new; Uncle Sam already offers grants, loans and tax credits to many students. The GI Bill provided World War II veterans with substantial tuition payments and living stipends; the United States military continues to offer similar programs. So-called Pell Grants are means-tested, higher education vouchers financed by the federal government.

The first advantage of vouchers over public higher education is that vouchers are readily means-tested. Since public higher education costs taxpayers more than $50 billion annually, current outlays could pay for full-tuition vouchers for about four million students – or more than one-third of those currently attending publics. Alternatively, a larger voucher covering living expenses as well as tuition could be provided to the poorest 5 to 10 percent, with the remaining funds used for middle-income students.

A key advantage of means-tested vouchers is that they make explicit the wealth transfers associated with publicly funded education. Today, the redistribution is not only perverse, but well hidden. And that makes it easier for politicians to play a game of musical chairs in

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which some middle-income taxpayers finance college for the children of other middle-income taxpayers.

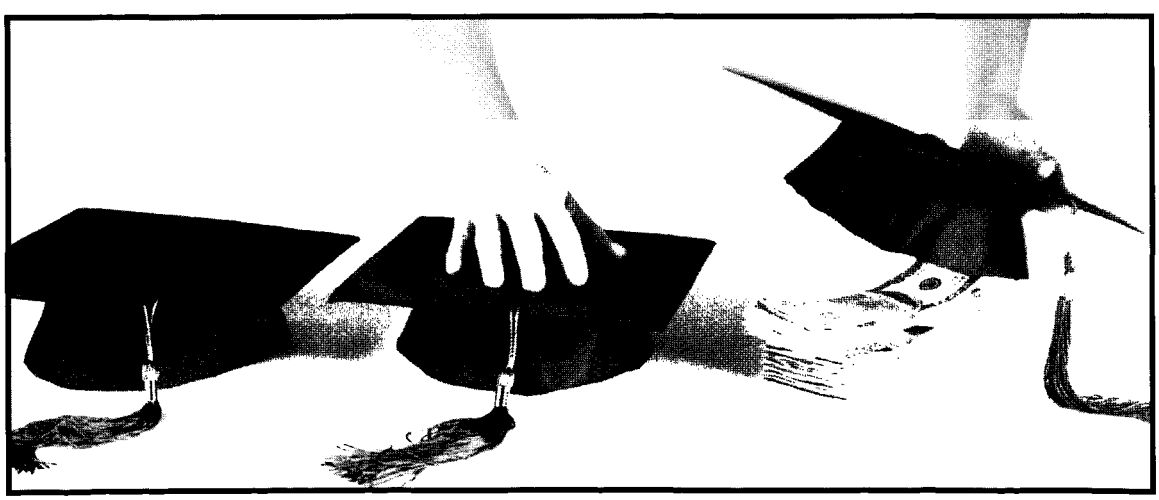
The second advantage of vouchers is that government is not compelled to resolve controversies regarding speech codes, single-sex institutions, affirmative action and the like. While access to vouchers could be conditioned on institutional policies – for example, non-discrimination on the basis of race – the indirect nature of the funding gives politicians cover in tolerating policies that offend some voters some of the time.

Thus, under vouchers, recipients might choose single-sex institutions, but there would be no public, single-sex institutions. Similarly, some recipients would choose institutions that practice affirmative action, while others would choose institutions that do not. Whether affirmative action would increase or decrease is an open question; it might increase if private colleges and universities find it attracts the students they want.

The final advantage of the voucher approach is that it relies entirely on private institutions to produce higher education. This reduces the potential for centralization, homogenization, and the stifling of innovation that is always a risk under public systems. As noted above, this has been only a modest problem in federalist America. But the greater market accountability and efficiency of privates relative to publics still argues for vouchers rather than public schools.

The fact that vouchers – or related policies such as subsidized loans – reduce the negative features of public higher education does not necessarily mean that vouchers are good policy. The most important negative is that vouchers require government to define what constitutes education, which can stifle innovation, impose homogeneity, and, in the extreme, control ideas. Thus the claim offered here is a qualified one: if subsidy for higher education makes sense, vouchers are a better method than public higher education. But voucher programs themselves require careful scrutiny.

The arguments against public education apply to schools at every level. And the caveats about vouchers apply as well. This paper has focused on higher education because I am an opportunist: society's presumption in favor of publics is weaker at this level, implying a greater willingness to entertain reforms from the ground up. M



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BY WILLIAM H. FREY

Regional demographic shifts have always been a driving force in shaping American politics. And the latest numbers released from the 2000 census, along with the startling results of last November's presidential election, suggest that the political landscape is once again changing in profound ways.

At the center of this change is the rise of what I call the New Sunbelt as a distinct political force. In recent decades, the conventional wisdom of political geography pitted largely Democratic, liberal-leaning cities against primarily Republican conservative suburbs. For decades, big city mayors and urban legislators catered to their minority, blue collar and labor union constituencies, while suburban politicians favored the causes of their mostly white middle class – notably the causes of lower taxes and greater local autonomy.

To be sure, there were regional nuances coloring this political divide. The conservative solid Democratic South gave way to the conservative solid Republican South, even as it held onto a distinct regional social perspective. By the same token, Northeasterners held more distinctly liberal regional points of view that differed sharply from the predilections and voting patterns of their socioeconomic counterparts in the right-leaning South, more independent West and middle-of-the-road Heartland states.

Yet within each region, the division between city and suburb formed a bright-line boundary. A suburban residence represented success for generations of families who aspired to a middle-class lifestyle they could share with neighbors who aspired to like values. This stood in contrast to the demographically heterogeneous urban polyglot – the very poor and very rich, minorities and immigrants, young professional singles and older retirees – all of whom lacked the desire or the wherewithal to locate in comfortable suburbs.

But the new census and recent election results suggest that suburbs are losing their collective identity. Largely middle-class white and African-American households are migrating from the old, congested, expensive suburbs of the Northeast and West Coast toward low-density communities of all sizes in the nation's Southeastern and less-urbanized Western states. Like the early suburbanites, these new regional migrants are looking for an easier lifestyle and co-residence with citizens who share their values and more middle-class political perspective.

At first glance, this migration might be seen as an extension of the long-term redistribution of population from the Frost Belt to the Sunbelt. But a closer look at the new census results, recent migration statistics and the

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November 2000 election suggests these movers are creating a new suburban-like category of states that can be termed the New Sunbelt. These states lie at the periphery of the historically prominent Sunbelt destinations: California, Texas and Florida. While these three states still attract migrants, they have become more urbanized. Their growth has been dominated by immigration from abroad, rather than from other parts of the United States. This is especially the case for California, which in recent years has lost more domestic migrants than it gained.

New Sunbelt states have drawn their new residents from other parts of the U.S., drawing the younger middle class and affluent baby boomers who hold middle-of-the-road views on social and economic issues. Their

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exodus from suburbs of more cosmopolitan, liberal-leaning urban areas on the coasts will forge clearer divides – demographic, cultural and political – between the states of the New Sunbelt and the more congested Melting Pot states in the old Sunbelt and Northeast.

The 2000 census highlights the ascendancy of these New Sunbelt states in terms of population. The fastest growing states of the 1990s were Nevada, Arizona, Colorado, Utah, Idaho and Georgia; each increased its growth rate significantly over the 1980s. North Carolina, another New Sunbelt star, increased its growth from 12 percent in the 1980s to 22 percent in the 1990s. Indeed, most of the New Sunbelt states accelerated their population growth substantially in the past decade.

The reapportionment of the House of Representatives in the wake of the new census also highlights their increased political importance. Seven of the 12 congressional seats that shifted between states went to the New Sunbelt: Arizona with two; Georgia with two; Nevada, Colorado and North Carolina with one each. The remaining five seats went to the premier old Sunbelt states: Texas, Florida, California. This is down from a collective gain of 14 seats that these three states enjoyed after the 1990 census-based reapportionment.

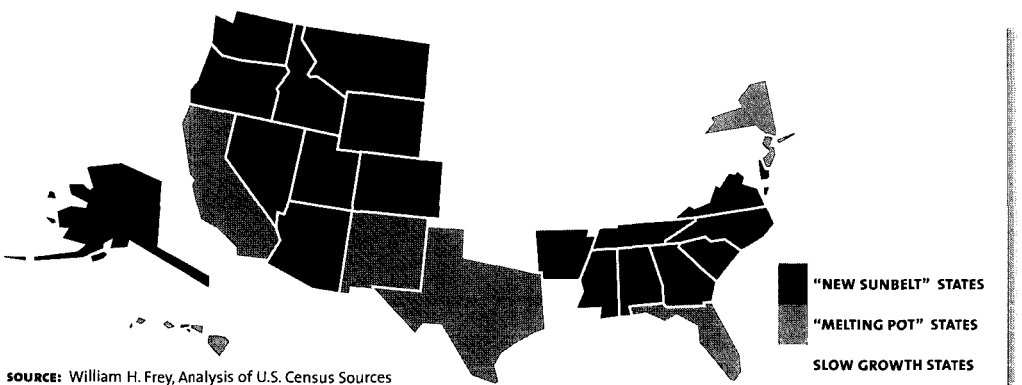
Moreover, in the recent presidential election all but three of the New Sunbelt states (Washington, Oregon, Delaware) favored the Republican candidate. Al Gore won most large Melting Pot states (California, New York and New Jersey, as well as New Mexico and Hawaii) and those in the slow-growing part of the country (Illinois, Pennsylvania, Michigan, Massachusetts and Connecticut as well as Maryland, Wisconsin, Minnesota, Iowa, Maine, Rhode Island and Vermont).

Our own analysis strongly implies that recent population movement patterns are contributing to the new political geography. It suggests that different constituencies will emerge in regions that we classify as the New Sunbelt, the Melting Pot states and the Slow Growing states that are located largely in the Snow Belt.

WHITE SHIFTS TO THE NEW SUNBELT

Since 1990, the white voting-age population

THE NEW POLITICAL GEOGRAPHY



SOURCE: William H. Frey, Analysis of U.S. Census Sources

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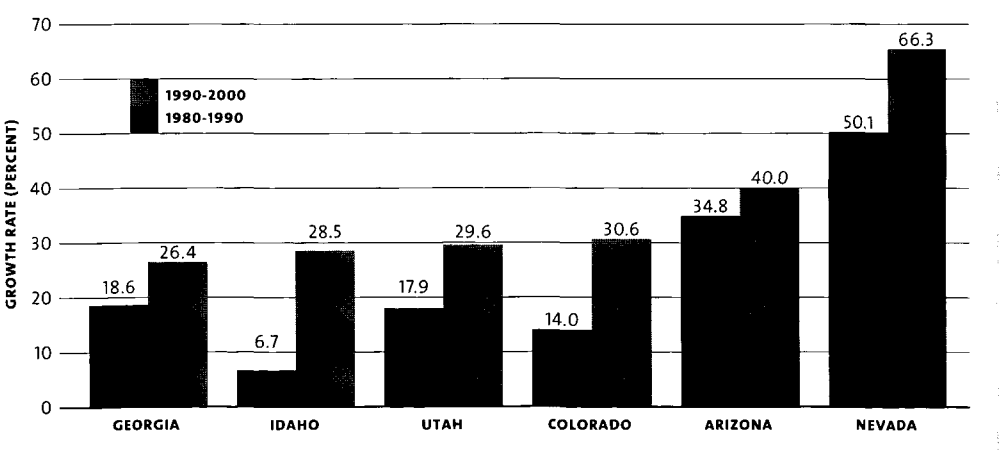
The fastest growing states of the 1990s were Nevada, Arizona, Colorado, Utah, Idaho and Georgia; each increased its growth rate significantly over the 1980s.

increased by more than 22 percent in each of these states: Nevada, Utah, Idaho, Arizona and Colorado. Thirty-six percent of the nation's gain in this group took place in the non-California west. Georgia, the Carolinas and Tennessee increased their white voting aged populations by 5.5 percent, more than twice the national rate.

The voters added to these New West and New South states come from all parts of the country, but the dominant origins are California and metropolitan New York. Indeed, from 1990 to 1999, California contributed to 71 percent of the "rest of the West" net white migration gains, while New York and New Jersey contributed to 65 percent of net white migration gains for South Atlantic states. They infuse new destinations with suburban demographic attributes that should reinforce middle-class moderate-conservative voting constituencies that already exist in those areas. The West is also noted for its attraction to young itinerant professionals who tend to be more independent – and libertarian – in their politics. A third group of new arrivals to both the West and Southeast are white retirees with some financial resources who, though economically conservative, like to be reassured about the solvency of the Social Security system.

While the white arrivals to both these New Sunbelt regions share middle-of-the-road values with the home-grown whites, their more cosmopolitan origins may make them more liberal on social issues and less opposed to gun control (in the West) or abortion (in

GROWTH IN NEW SUNBELT STATES



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the South). In the latter region, the influx of new suburban whites is accompanied by another new influx that should serve to moderate the social tenor of political discourse: the return of blacks from the North.

BLACKS GO SOUTH

The 1990s represented something of a full-circle shift in black migration, countering the trend of most of the last century. More blacks from the other census regions (Northeast, Midwest and West) moved to the South than left the region. Between 1990 and 1999, the South picked up a net gain in black voting-aged migrants of 326,000 from the rest of the United States. Indeed, on Election Day 2000, 53 percent of the nation's black voting-age population resided in the South. Several subgroups made up this movement: middle-class blacks drawn to the vibrant New South economies, working-class blacks who were turned away from manufacturing restructuring in the North, and black retirees who are more likely to relocate in southern communities than those in the West.

Yet, it is the increasing numbers of baby boomer professional blacks who will moderate the tone of both Republican and Democratic appeals on middle-of-the-road economic issues and away from the thinly disguised racial politics of the past. While African-American newcomers will certainly be receptive to traditional black Democratic constituency issues like affirmative action, the middle-class among these newcomers will

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The re-consolidation of blacks in the South, along with in-migration of northern suburban whites, won't blur the South's distinct regional politics, but it will make these states more progressive.

also be receptive to more moderate proposals like targeted tax cuts, school vouchers and partial privatization of Social Security. By the same token, the new white migrants will be less likely to side with long-time residents on conservative cultural issues.

The reconsolidation of blacks in the South, along with in-migration of northern suburban whites, won't blur the South's distinct regional politics, but it will make these states more progressive. The Southern states we have classed as part of the New Sunbelt are emblematic of these new trends. On Election Day 2000, their voting-age population was 22 percent black, 74 percent white and less than 4 percent Hispanic and Asian.

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MELTING POT STATES

Surely, the most dramatic migration-related change in the nation's electorate since 1990 was the infusion of new immigrant minorities. Between the last two censuses the combined voting-age populations of Hispanics and Asians increased by 9.6 million, to 29.5 million over all. Moreover, the impact of the increase was magnified by their concentration in a handful of states. California, Texas, Florida and New York garnered 61 percent of these gains and are now home to almost two-thirds of the combined Hispanic and Asian population. We call these states, along with New Jersey, Hawaii and New Mexico, the Melting Pot states. Here, non-Hispanic whites represent only 61 percent of potential voters, while Hispanics and Asians constitute 29 percent of voting-age residents.

It is true that new immigrant minorities tend to vote in significantly lower numbers than the remaining population. Nonetheless, both George Bush and Al Gore paid attention to the changing demographics when visiting Melting Pot states – both symbolically, by speaking Spanish when visiting Hispanic neighborhoods, and in their policy prescriptions, by favoring reforms in the Immigration and Naturalization Service, improved public education and support for family values. Both

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were aware of California's drastic Republican-to-Democratic shift in state offices, which was attributed in part to the perceived anti-immigration sentiment of the former Republican governor Pete Wilson. The beat goes on: Hispanic and Asian share of the Golden State's voting-aged population is projected to increase from 40 percent in November 2000 to 52 percent in 2015.

Immigration is not the only cause for the rise of Hispanic and Asian visibility in the Melting Pot states. New York, New Jersey and California exhibited a decline and out-migration of their white voting-age populations over the course of the 1990s. In large measure this reflects the exodus to the New Sunbelt, and this helps to cement differences in the constituencies of both groups of states.

More than in the past, presidential candidates' speeches, public service announcements and debates are seen nationwide, and they play quite differently in one area from another.

SLOW GROWING STATES

Much attention has been paid to the dominant-destination states for immigrants, white suburbanites and African-Americans. Still, there is a broad swath of states in the interior of the country whose population gains have been relatively modest or nil. The voting-age population of each has grown slower than the national rate of 11.4 percent between the 1990 census and Election Day 2000.

These slow-growing and declining states were important in the last election and will remain important to building winning electoral coalitions. One reason is that they are strategic states; despite George W. Bush's victories in Texas and Florida, most Melting Pot states are likely to tilt toward Democrats on liberal issues. Similarly, the changing demographics of the New Sunbelt states are likely to keep them in the columns of more moderate and conservative Republican candidates. The swing states are thus likely to include a number of what we label Slow Growing states.

Further, key demographic segments that were recently designated to be important "swing voter" groups have a disproportionate weight in these states. This is because the demography of Slow Growing states exaggerates the importance of groups who have not moved to faster-growing parts of the country. Thus, they are home to older, whiter and more middle-income populations than other parts of the country.

Swing-voter groups with a large presence in these states include white working wives, white "forgotten majority" men and white seniors. According to Ruy Teixeira and Joel Rogers, authors of *America's Forgotten Majority: Why the White Working Class Still Matters* (Basic Books, 2000), these groups seem to have been lost in the shuffle as more attention was paid to upscale "soccer moms" in the 1992 and 1996 presidential races. Major presidential contenders court these groups by emphasizing "compassionate" policies or a

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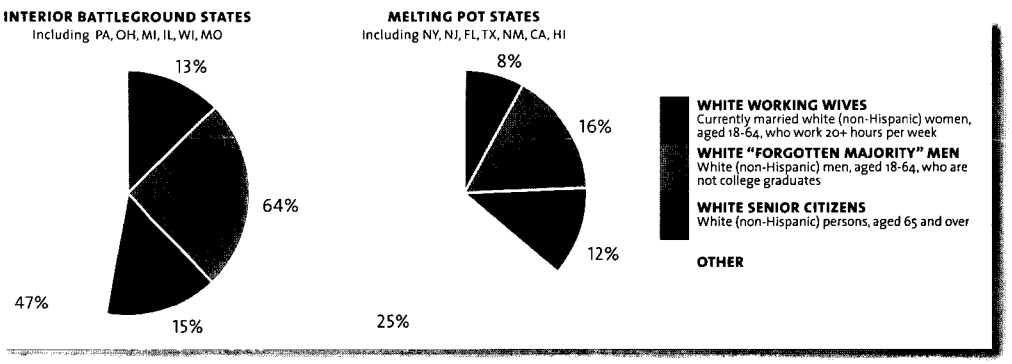
willingness to fight for "working class families." White seniors, the third group, tend to vote in disproportionately high percentages. Their vote was also courted by both candidates in 2000 – hence the high profile of Social Security and Medicare prescription drug insurance.

From a demographic perspective, the significance of all three groups is inflated because they reside in swing states from which disproportionate numbers of younger, minority or more upscale groups have moved away. This can be seen by looking at the share of each of these three groups in the combined voting populations of six "battleground" states (Pennsylvania, Ohio, Michigan, Illinois, Wisconsin and Missouri) in the 2000 election. Together, the three groups represented 53 percent of the voting-aged population of these states. By contrast, they constitute only 36 percent of the voting-aged population of Melting Pot states and only 46 percent of the total United States voting-age population.

HOW SHARES OF KEY DEMOGRAPHIC GROUPS DIFFER ACROSS STATES (VOTING-AGED POPULATIONS, 1999)



THE NEW REGIONAL POLITICS

Recent migration and immigration patterns are shaping new demographic divides now emerging. The directed destinations of middle-class and upscale white suburbanites to the New Sunbelt, the migration of blacks to the South, the clustering of new ethnic minorities in Melting Pot states, and an expanded number of interior Slow Growing states with increasingly older, whiter populations, are creating regional divides with distinct sets of constituencies and issues. More than in the past, presidential candidates' speeches, public service announcements and debates are seen nationwide, and they play quite differently in one area from another.

No wonder the presidential candidates were careful in crafting their messages so as not to offend important groups within different regions. Who could object to a candidate claiming to be "a uniter and not a divider"? Or one who is not afraid to display traditional family values, via frequent public displays of affection with his spouse? In the politics of the future, with the regions becoming more demographically distinct, national presidential campaigns will become ever more delicate balancing acts. M

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EKED INTO OFFICE BY BUTTERFLY-BAFFLED SENIORS MISTAKENLY VOTING FOR THE OPPOSITE OF WHAT THEY'D INTENDED, THE NEW PRESIDENT VOWED TO CARRY OUT HIS MANDATE.

I PLEDGE TO DO THE OPPOSITE OF WHAT THE MAJORITY THOUGHT THEY WERE VOTING FOR!

HE WAS A MAN OF CLEAR CONVICTIONS.

OUR SURPLUS DOES NOT BELONG TO GOVERNMENT. MOST OF IT BELONGS TO RICH PEOPLE!

I REALIZE MY TAX CUTS WILL DRAIN MEDICARE AND DELAY SOCIAL SECURITY REFORM, BUT THOSE CRISES WON'T EXPLODE UNTIL THE BOOMERS RETIRE IN TEN OR FIFTEEN YEARS.

ALL I NEED TO WORRY ABOUT ARE THE NEXT EIGHT!

SURELY THE WISE FED CHAIRMAN-SEEING THE BIGGER PICTURE - WOULD TALK SOME SENSE TO THE IDEOLOGICALLY BLINDED PRESIDENT.

OR WOULD HE?

MASSIVE TAX CUTS SOUND GREAT! I HATE GOVERNMENT TOO! VIVA AYN RAND!

I'M TIRED OF PRETENDING I CARE ABOUT AVERAGE AMERICANS. I'M RICH, AFTER ALL, AND SO ARE MY FRIENDS. AND I WANT MY FRIENDS TO BE HAPPY.

BUT SUDDENLY HE WAS CRITICIZED, KNOCKED OFF HIS PEDESTAL, ACCUSED OF BEING "POLITICAL".

MAYBE IF I BACKTRACK A LITTLE, I CAN REGAIN MY MYSTIQUE!

ONLY IN PRIVATE COULD HE ADMIT THE TRUTH.

I'VE NEVER BELIEVED IN DEBT REPAYMENT OR FISCAL RESPONSIBILITY. IRRESPONSIBLE TAX CUTS ARE FINE BY ME.

ALOOFNESS... MALLEABILITY... WHATEVER IT TAKES, ...

I JUST WANT TO BE LOVED.

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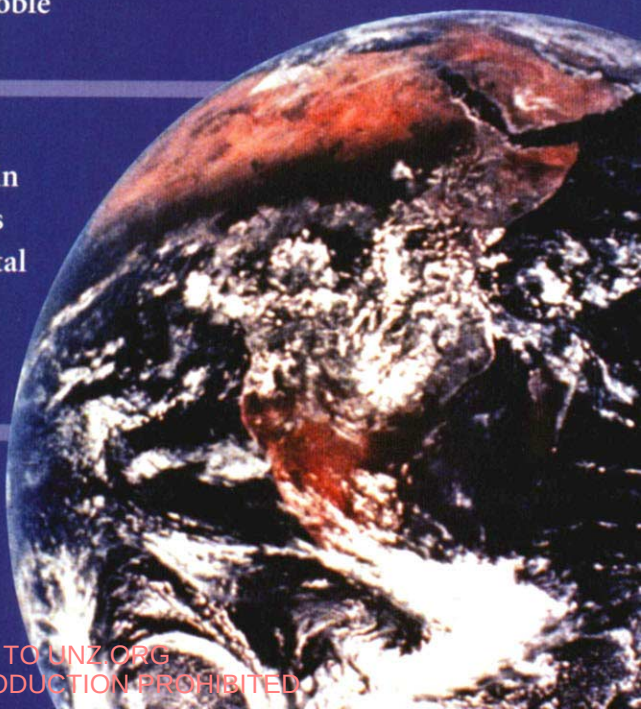

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Can't tell the players without a scorecard.

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A cartoon strip by
MARK ALAN STAMATY,
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